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No.

In the Supreme Court of the United States

OCTOBER TERM, 1980

UNITED STATES OF AMERICA, PETITIONER

v.

STATE OF NEW MEXICO, ET AL.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE TENTH CIRCUIT

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QUESTION PRESENTED

Whether contractors of the United States Department of Energy, engaged for the management and operation of government-owned atomic research laboratories, are agents of the United States so that payments made by the contractors with funds of the federal government to procure goods and to pay for the operational costs of the laboratories are constitutionally immune from the New Mexico gross receipts and compensating use taxes.

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*In addition to the State of New Mexico, the other respondents herein are the Bureau of Revenue of the State of New Mexico, and Fred L. O'Cheskey, as Commissioner of Revenue of and for the State of New Mexico.

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The Solicitor General, on behalf of the United States of America, petitions for a writ of certiorari to review the judgment of the United States Court of Appeals for the Tenth Circuit in this case.

OPINIONS BELOW

The opinion of the district court (App. A, *infra*, 1a–10a) is reported at 455 F. Supp. 993. The opinion of the court of appeals (App. B, *infra*, 11a–28a) is reported at 624 F.2d 111.

JURISDICTION

The judgment of the court of appeals (App. C, *infra*, 29a–30a) was entered on June 2, 1980. By orders of August 15, and September 19, 1980, Mr. Justice White extended the time within which a petition for a writ of certiorari could be filed to and including October 30, 1980. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

STATUTE INVOLVED

The pertinent parts of New Mexico's Gross Receipts and Compensating Tax Act, N.M. Stat. Ann. 1953, §§ 72-16A-3, 72-16A-4, 72-16A-7, 72-16A-12, 76-16A-12.1, 72-16A-12.2, 72-16A-14, and 72-16A-14.9 (Supp. 1975), are set forth in App. D, *infra*, 31a–34a.

STATEMENT

1. Sandia Corporation was organized in 1949 as a special subsidiary of Western Electric Company, Inc., for the purpose of performing research and development for the United States Atomic Energy Commission (now the Department of Energy—DOE) in New Mexico. It is not involved in any private work, receives no fee or profit under its contract, and owns no property except the $1,000

in United States bonds that constitutes its paid-in capital (App. A, *infra*, 3a).

The Zia Company is a subsidiary of Santa Fe Industries, Inc. Since 1946, Zia has performed a variety of management, operational, maintenance, architect-engineer, procurement, and related functions in connection with DOE's Los Alamos Scientific Laboratory. Zia performs separate private work with a distinct set of records, employees and locations. Virtually none of Zia's private property is involved in performance of its contract with DOE (App. A, *infra*, 3a; App. B, *infra*, 14a).

Los Alamos Constructors, Inc. (LACI) is a subsidiary of the Zia Company. It performs construction work in support of the Los Alamos Scientific Laboratory. LACI owns no property and makes no purchases. Rather, it procures the property it needs for performance of its Los Alamos contract through Zia. Zia and LACI are paid fixed fees annually for work performed under their contracts with DOE (App. A, *infra*, 3a; App. B, *infra*, 14a).

The management contracts between DOE and Sandia, Zia, and LACI are standard Atomic Energy Commission (now DOE) management contracts. This type of contract was developed to facilitate the Atomic Energy Commission's heavy reliance on private industry in the construction and management of large research and development facilities (App. B, *infra*, 13a). The standard DOE management contract provides that title to all tangible personal property passes directly to the government from the vendor. Thus, the contractors do not own any of the tangible personal property they procure. Moreover, the contract also places the risk of loss upon the government for property procured under the contracts. Finally, the contract provides for government control over the disposition of the property and government approval of property management procedures employed by each contractor (App. A, *infra*, 4a).

The tangible personal property procured by Sandia and Zia and all other operational costs incurred under the contracts, such as salaries, are paid for under an "advanced

funding" procedure. Under this procedure, the contractors pay their vendors and employees with drafts drawn directly on United States Treasury funds maintained in a depository bank account, under the authority of a letter of credit to cover withdrawals (App. A, *infra*, 4a).

The "advanced funding" procedure involves the establishment of a special bank account by the contractor, the United States, and a designated bank, pursuant to a three-party contract. The United States owns any balance in the account, but the contractor has the right to execute drafts payable to third parties in order to pay any expenses incurred in performing the underlying government contract. DOE thereupon issues a letter of credit to an appropriate Federal Reserve Bank in favor of the contractor. The letter of credit provides the general authority for the Federal Reserve Bank to make United States Treasury funds available for deposit in the special bank account. When a contractor incurs an expense under the contract, it pays the expense by executing a draft payable to the creditor and drawn on the special bank account. At the same time, the contractor or the bank executes a payment voucher in an amount sufficient to cover the draft and the Federal Reserve Bank, on the basis of the voucher, transfers funds into the special bank account (App. B, *infra*, 22a n.8).

Under the contract, the government owns the funds in the special accounts and controls the disposition of such funds. The liability provisions of the contract require the government to pay all operational costs and further stipulate that no contractor funds are to be used to pay for contract costs. Obligations that are "properly incurred" by the contractors are therefore considered to be DOE liabilities. Hence, if the government failed to provide funding, the contractors would be excused from performance of the contracts and the government would be liable for all properly incurred and reported claims (App. A, *infra*, 4a-5a).

Prior to July 1, 1977, DOE's contracts with Sandia, Zia, and LACI did not characterize the contractors as "agents"

of the government. On that date (which was during the pendency of this litigation), the contracts were modified to recognize the "'long standing agency status and authority' of the contractors 'for certain purposes'" (App. A, *infra*, 6a). The amendments also stated that they "shall not be construed to modify any other provisions of the contract * * * nor shall [they] create rights or obligations not otherwise provided for in the contract" (App. B, *infra*, 26a).

2. The New Mexico gross receipts tax is levied upon sales proceeds realized by retailers of tangible personal property (a sales tax) and upon the gross receipts realized by persons engaged in the construction business or in performing services of a professional, technical, or scientific nature. There is also a compensating tax equivalent to the gross receipts (sales) tax that is imposed upon the use of tangible personal property that has been imported into and used within the State without the payment of any gross receipts (sales) taxes. See App. D, *infra*, 31a-34a.

Prior to 1967, the New Mexico Bureau of Revenue acknowledged the existence of an agency relation between these contractors and the United States and imposed no taxes on the type of transactions involved in this case. In 1967, however, the State changed its position with respect to the relationship between the contractors and the government sought to impose such taxes on the ground that the contractors were not government agents (App. A, *infra*, 6a).

The government thereafter brought this action in the United States District Court for the District of New Mexico for a declaratory judgment that sales of tangible personal property to DOE, through its management contractors Sandia and Zia, are sales to the United States that are exempt from the New Mexico gross receipts and compensating taxes, and that the advanced funds disbursed under the management contracts here are not subject to such taxes (App. A, *infra*, 1a-2a; App. B, *infra*, 11a-12a).

3. The district court concluded "that Sandia and Zia are procurement agents of the United States and that any sales of tangible personal property to them are sales to the United States through its procurement agents, which are not subject to the 4% gross receipts tax imposed by the New Mexico Gross Receipts and Compensating Tax Act" (App. A, *infra*, 7a). It also held that the contractors were not subject to the compensating tax for their purchases of tangible personal property in other states (*ibid.*).

Finally, the district court held that the advanced funds disbursed by Sandia, Zia and LACI were not compensation for services subject to the New Mexico gross receipts tax but were funds that belonged to the government and were disbursed by the contractors to pay operational costs. In support of this conclusion, the district court observed that Zia and LACI received a fixed fee as compensation for their services, upon which they paid gross receipts taxes, and that Sandia received no fixed fee or profit. Moreover, the court pointed out with respect to the advanced funds procedure that the funds deposited by DOE in the special bank accounts were the only monies available for payment of all of the contractors' operational costs. They were not to be disbursed in any manner inconsistent with contract performance. DOE could exert direct control over the disbursement of the funds and retained title to the funds while they were on deposit with the bank (App. A, *infra*, 8a-9a). Accordingly, the district court upheld the government contractors' immunity from New Mexico gross receipts and compensating use taxes and entered a declaratory judgment in favor of the government (*id.* at 10a).

4. The court of appeals reversed (App. B, *infra*, 11a-28a). It held that Sandia, Zia and LACI were not agents of the United States and were therefore subject to New Mexico gross receipts and compensating use taxes. After reviewing this Court's decisions dealing with the state tax immunity of government contractors, the court of appeals acknowledged that "[a]lthough there is language in these Supreme Court opinions suggesting that the results turn on traditional agency principles * * *, it seems evident

that the Court is more concerned with preserving the delicate financial balance between our co-existing sovereignties than with rigid adherence to agency law terminology" (App. B, *infra*, 17a). The court of appeals further observed that "[t]he trend toward restricting tax immunities * * * reflects an awareness of the serious threat posed to state revenues by ballooning governmental dealings in the private sector" (*ibid.*).

In holding that the contractors were not agents, the court of appeals attempted to distinguish two decisions of this Court—*Kern-Limerick, Inc.* v. *Scurlock*, 347 U.S. 110 (1954), and *Livingston* v. *United States*, 364 U.S. 281 (1960) (per curiam), aff'g 179 F. Supp. 9 (E.D.S.C. 1959) (three-judge court)—which upheld the immunity of contractors from state sales taxes on the ground that they were agents of the government. As the court of appeals viewed the matter, the language in the request for bids, the contract, and the purchase order in *Kern-Limerick* more "clearly and uniformly disclosed an intention for the government to be directly obligated to the vendor for the contractor's purchases" (App. B, *infra*, 15a). Moreover, the court sought to distinguish *Livingston* on the ground that the contractor in that case earned no fee (*id.* at 16a), although in considering the fact that Sandia likewise earned no fee, the court of appeals "decline[d] to hang agency status, and thereby the welfare of state treasuries, on the existence or amount of a fee" (*id.* at 25a).

Finally, the court rejected the government's argument that the advanced funding procedure conclusively established that Sandia, Zia and LACI were procurement agents that pledged the credit of the United States vis-a-vis the third-party vendors. In the court's view, "[a]dvanced funding is simply another means of reimbursement devised by accountants to eliminate major weaknesses in the government's bookkeeping practices" (*id.* at 23a).

REASONS FOR GRANTING THE PETITION

In holding that government contractors, engaged to manage government-owned atomic research laboratories

and to procure property for such purposes with funds advanced by the federal government, were not agents of the United States and were therefore subject to state gross receipts taxes, the decision of the court of appeals represents a fundamental departure from the governmental tax immunity precedents of this Court, *viz.*, *Kern-Limerick, Inc.* v. *Scurlock*, 347 U.S. 110 (1954), and *Livingston* v. *United States*, 364 U.S. 281 (1960) (per curiam), aff'g 179 F. Supp. 9 (E.D.S.C. 1959). Moreover, the decision below squarely conflicts with *United States* v. *Boyd*, 211 Tenn. 139, 363 S.W. 2d 193 (1962), aff'd on another issue, 378 U.S. 39 (1964), and *United States* v. *Nevada Tax Commission*, 439 F.2d 435 (9th Cir. 1971), aff'g 291 F. Supp. 530 (D. Nev. 1968).

The issue is important to the Department of Energy because it maintains numerous contractual relationships with private parties engaged in operating federally-owned laboratories devoted to research, development, and production of nuclear material and devices. Under these standard DOE contracts, the United States must pay all operational costs of the laboratories, including all state taxes. The sums involved are indisputably substantial. If the decision below stands, the Department of Energy estimates that it will owe more than $100 million to the State of New Mexico for the years from 1970 to date, and $20 million annually for future years. When these figures are extrapolated over the large number of agreements DOE has outstanding with other private contractors to perform services in this vital field of scientific research, the fiscal impact of the question presented assumes even greater significance.

Under the present state of the decisional law, the court below, on the one hand, and the Ninth Circuit and the Supreme Court of Tennessee, on the other hand, have adopted opposing views as to whether the standard DOE management contract immunizes the contractor from state sales taxes under *Kern-Limerick*. Tennessee (where DOE maintains substantial facilities) and states in the Ninth Circuit (such as Nevada and California) may not impose

and collect such taxes, but those in the Tenth Circuit such as respondent New Mexico are free to do so. Such a situation is fundamentally unfair. There should be a uniform national rule to which all the states and the federal government should be bound regarding the state tax consequences of the operations under such an important federal contract. This Court should resolve the conflict of decisions and thereby establish uniform immunity rules for the guidance of the state tax authorities, the federal government, and its contractors.

1.a. In *McCulloch* v. *Maryland*, 17 U.S. (4 Wheat.) 316 (1819), this Court first announced the doctrine that the federal government is immune from state taxation. "[U]nshaken, rarely questioned * * * is the principle that possessions, institutions, and activities of the Federal Government itself in the absence of express congressional consent are not subject to any form of state taxation." *United States* v. *County of Allegheny*, 322 U.S. 174, 177 (1944). See also *Department of Employment* v. *United States*, 385 U.S. 355 (1966); *United States* v. *Mississippi Tax Commission*, 421 U.S. 599, 612-613 (1975). Federal tax immunity is "the unavoidable consequence of that supremacy which the constitution has declared." *McCulloch* v. *Maryland*, *supra*, 17 U.S. (4 Wheat.) at 436.

In determining the reaches of the federal government's constitutional immunity from state taxation, this Court has often extended the doctrine to protect private contractors who act on behalf of the United States. Thus, prior to *Alabama* v. *King & Boozer*, 314 U.S. 1 (1941), it had been held that a private contractor could not be subject to state taxation in connection with his performance of a government contract if he could pass the cost of the tax on to the federal government. However, in *King & Boozer* the Court abandoned this "economic burden" test and ruled that federal sovereignty "does not spell immunity from paying the added costs, attributable to the taxation of those who furnish supplies to the Government and who have been granted no tax immunity" (314 U.S. at 9). There, however, the legal incidence of the tax was on the

private vendors, and the contracts provided that the contractor was to purchase the materials in its own name and on its own credit. The government was not bound by the contractors' purchase contracts but would reimburse the contractor only after the goods were delivered and inspected. In those circumstances, the Court concluded that the government's prerogatives under the contracts did not confer upon the contractor the status of an agent empowered to pledge the credit of the United States (see *id.* at 13).

Kern-Limerick, Inc. v. *Scurlock*, *supra*, employed the Court's earlier analysis in *King & Boozer* in holding that a federal contractor was entitled to immunity from state sales tax if it was an agent of the federal government empowered to pledge the credit of the United States. There, the Court held unconstitutional the Arkansas sales tax as applied to purchases by a government contractor under a cost-plus-fixed fee contract, where the pertinent documents made it clear that the contractor was acting as a purchasing agent for the government, title to the goods purchased passed directly from the vendor to the government, and the government was directly liable for payment of the purchase price. Accordingly, the Court concluded that "the Government is the disclosed purchaser and that no liability of the purchasing agent to the seller arises from the transaction" (347 U.S. at 121; footnote omitted).

b. The decision rejecting the claimed immunity of the contractors in this case is difficult to square with *Kern-Limerick*. Here, as in *Kern-Limerick*, the DOE management contracts to which Sandia, Zia and LACI were parties provided that title to all tangible personal property passed directly to the government from the vendors, as well as placing the risk of loss directly on the government for property acquired under the contracts. The contracts further provided for government control over the disposition of the property and approval of property management procedures employed by each contractor. Finally, the advanced funding arrangement, under which the contractors did not expend any of their own funds for goods or serv-

ices but were able to disburse monies that at all times belonged to the government, "gave to the contractors the status of agents of the Government to enter into contracts or to pledge its credit." *Alabama* v. *King & Boozer*, *supra*, 314 U.S. at 13. As the Fourth Circuit correctly observed in *United States* v. *Forst*, 569 F.2d 811 (1978), "the key factor in the case was whether the credit of the United States or the contractor was bound by the purchasing agreements" (*id.* at 811). Since Sandia, Zia, and LACI were empowered to write checks on government-owned funds, their power to bind the United States and pledge its credit cannot seriously be questioned.

Contrary to the court of appeals' conclusion, the advanced funding procedure cannot be dismissed as "simply another means of reimbursement devised by accountants * * *" (App. B, *infra*, 23a). There is a considerable difference between the case where the contractor expends its own funds and must await reimbursement by the government and the case in which the contractor is empowered to draw directly on the funds of the government. While the former case may not be inconsistent with an agency relationship (as *Kern-Limerick* itself demonstrates), it is at least clear that in such a case the contractor must rely upon the government's ratification of its actions in order to obtain reimbursement for its outlays. Here, on the other hand, the contractors did not even take that risk, for they disbursed *government* funds to the vendors and to their employees in the first instance. In every sense of the word, the contractors here acted on behalf of the government vis-a-vis the vendors. If the contractor receiving after-the-fact reimbursement in *Kern-Limerick* was deemed to be an agent of the United States and thereby immune from state taxes, there is, in this respect at least, a stronger case for immunity here because the contractors had the additional authority to disburse government-owned funds and pledge the credit of the United States.

Although the court of appeals acknowledged that this created "appearances" of agency status for the contractors (App. B, *infra*, 22a), it resisted the conclusion that the

contractors were immune from state taxes, relying on the fact that "[a]t most, the contractor may pledge to the limit of its letter of credit" (*id.* at 22a-23a). As the court reasoned, "[s]een in this light, Sandia, Zia and LACI are like numerous businesses which deal under letters of credit from banks and other sureties" (*id.* at 23a).

But the conclusion that the contractors' purchases and disbursements were subject to state gross receipts taxes does not follow from the fact that their letters of credit were limited in amount. The claim of immunity here is only coextensive with the contractors' authority to act on behalf of the government. The fact that their authority was limited in dollar amounts does not refute the argument that they acted as agents of the government within the scope of their authority. Indeed, it requires no citation of authority that the acts of an agent are attributable to his principal to the extent they are within the scope of the agent's authority. Simply because there is some limit upon the agent's authority does not cast doubt upon the existence of the agency relationship itself.

c. The decision below also conflicts with *Livingston* v. *United States*, *supra*. There, this Court summarily affirmed a three-judge district court's decision that a South Carolina sales tax could not be imposed upon a contractor's purchases under a similar DOE standard management contract. The court of appeals sought to distinguish the case on the ground that it turned on the fact that the contractor earned no fee from the contract (App. B, *infra*, 16a), in much the same fashion as this Court distinguished *Livingston* in *United States* v. *Boyd*, *supra*, 378 U.S. at 45 n.6. However, the court of appeals also expressed doubt that "such a factual determination would today withstand appellate review" (App. B, *infra*, 24a; footnote omitted) and therefore "decline[d] to hang agency status, and thereby the welfare of state treasuries, on the existence or amount of a fee" (*id.* at 25a).

But whatever the merits of such a distinction, the undisputed fact is that Sandia received no fee or profit under

its contract with DOE (App. A, *infra*, 3a). Hence, a square conflict with *Livingston* exists at least to the extent of New Mexico's power to impose its tax on Sandia.

2. Nor does the fact "that the agency terminology does not appear uniformly in all the documents relating to the contracts" (App. B, *infra*, 26a) effectively distinguish this case from *Kern-Limerick*, as the court of appeals apparently believed. Much the same argument was advanced by the State of Tennessee and rejected by the Tennessee Supreme Court in *United States* v. *Boyd*, 211 Tenn. 139, 363 S.W.2d 193 (1962), aff'd on another issue, 378 U.S. 39 (1964). There, the Tennessee court held that the contractor under the identical standard DOE management contract with advanced funding was immune from state sales taxes. In response to the argument that the contract did not in all respects employ the identical *Kern-Limerick* terminology of "agency," the court stated, in terms that are equally appropriate here (211 Tenn. at 155; 363 S.W. 2d at 200):

> The mere placing of terms such as agent or independent contractor in the contract does not make them such in law. The surrounding facts and circumstances determine the relationship.
>
> It appears from the contract and from the actions of the parties that the relationship of agency in so far as the purchase of materials are [*sic*] concerned when accomplished in accordance with the contract bring them within the holding of Kern-Limerick and under that case the A.E.C. is the purchaser. Therefore, the Sales Tax would be a direct tax upon the Government and is invalid under the doctrine of implied immunity, and we so hold.

Boyd therefore likewise conflicts with the decision below.[1]

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[1] The conflict upon which we rely between the decision below and *Boyd* is with the sales tax portion of *Boyd* that was considered by the Tennessee Supreme Court, which the State did not appeal to this Court (see 378 U.S. at 43 n.5). The issue before this Court was the constitutionality of the state use tax as applied to the contractor. This Court affirmed the Tennessee Supreme Court's holding that the State

3. Finally, the decision below squarely conflicts with *United States* v. *Nevada Tax Commission*, 291 F. Supp. 530 (D. Nev. 1968), aff'd, 439 F.2d 435 (9th Cir. 1971), a case that the court of appeals here conspicuously ignored. There, as here, the state sought to impose its sales and compensating use tax upon a government contractor's purchase and use of tangible personal property under the identical standard DOE contract. In accordance with the advanced funding procedure, the contractor purchased the property with government-owned funds, and title to the property vested immediately in the government. Relying on *Kern-Limerick*, the district court upheld the contractor's claim that the sales were immune from a comparable Nevada sales and compensating use tax modeled after a California statute. As the court there concluded, "all sales by retailers to [the contractor] under this contract, the purchase price being paid by the Government and title passing immediately to the Government, are sales to the United States immune from the Nevada Sales Tax" (291 F. Supp. at 533). The Ninth Circuit simply affirmed "[f]or the

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could impose a tax on a government contractor on the use of tangible personal property in the performance of a contract because the contractor had not been "so incorporated into the government structure as to become instrumentalities of the United States and thus enjoy governmental immunity" (*id.* at 48).

Contrary to the court of appeals' conclusion (App. B, *infra*, 20a n.7), this Court's use tax holding in *Boyd* does not support its ruling that Sandia, Zia, and LACI were not agents and therefore not immune from the New Mexico sales tax. The Tennessee use tax at issue in *Boyd* was not a compensating use tax of the type involved in this case, which is meant to complement a sales tax by levying a tax upon out-of-state purchases. See, *e.g.*, *General Trading Co.* v. *State Tax Commission*, 322 U.S. 335, 336–337 (1944). Rather, the Tennessee use tax was imposed upon the use of property as a privilege irrespective of the title of the property or its importation (see 378 U.S. at 40–41 n.3). This type of use tax was considered and upheld by the Court in the so-called "Michigan cases." See *United States* v. *City of Detroit*, 355 U.S. 466 (1958); *City of Detroit* v. *Murray Corp. of America*, 355 U.S. 489 (1958); and *United States* v. *Township of Muskegon*, 355 U.S. 484 (1958). Hence, the court of appeals' reliance on this Court's use tax holding in *Boyd* is entirely misplaced.

reasons stated in the reported decision of the district court" (439 F.2d at 441).

Finally, the court of appeals stated that it was "highly skeptical of the sporadic addition of 'magic words' to a contract in an attempt to avoid state taxation" (App. B, *infra*, 26a). But this Court in *Kern-Limerick* harbored no such doubts. In that seminal decision, from which the court below departed, this Court concluded that "the form of contracts, when governmental immunity is not waived by Congress, may determine the effect of state taxation on federal agencies, for decisions consistently prohibit taxes levied on the property or purchases of the Government itself" (347 U.S. at 122–123; footnotes omitted). The confusion that has arisen in the lower courts about the meaning of *Kern-Limerick*, which will produce discrepancies in the ability of various states to tax essentially identical transactions, calls for review by this Court.

CONCLUSION

The petition for a writ of certiorari should be granted.

Respectfully submitted.

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OCTOBER 1980

APPENDIX A

United States District Court

DISTRICT OF NEW MEXICO

No. 75-48-M

[Filed August 4, 1978]

UNITED STATES OF AMERICA, PLAINTIFF

v.

STATE OF NEW MEXICO, BUREAU OF REVENUE OF THE STATE OF NEW MEXICO, AND FRED L. O'CHESKEY, AS COMMISSIONER OF REVENUE OF AND FOR THE STATE OF NEW MEXICO AND HIS SUCCESSORS IN OFFICE, DEFENDANTS.

MEMORANDUM OPINION

MECHEM, *District Judge.*

This matter is before the Court on cross-motions for summary judgment. The parties are in agreement that there is no genuine issue of material fact, and I find that it is proper to grant summary judgment in favor of the plaintiff on the basis of the law and the affidavits, exhibits, depositions and interrogatories on file in this case. The following shall constitute my findings of fact and conclusions of law. Jurisdiction exists over the parties and the subject matter.

In this action the United States is seeking a declaratory judgment that, in light of the Constitution and the laws of the United States and New Mexico:

1. Sales of tangible personal property to Energy Research and Development Administration (ERDA), through its management contractors, Sandia Corporation (Sandia) and the Zia Company (Zia), are sales to the United States which are not subject to the 4% gross receipt tax nor to the compensating tax imposed by the New Mexico Gross Receipts and Compensating Tax Act; and

2. U.S. Government advanced funds used for Government operations under ERDA management contracts with Sandia, Zia and Los Alamos Constructors, Inc. (LACI), are not subject to the 4% gross receipts tax imposed by the New Mexico Gross Receipts and Compensating Tax Act; and

3. The United States has the right to be a party to administrative tax proceedings before the New Mexico Commissioner of Revenue wherein tax liabilities of the contractors or their vendors are at issue.

The State Bureau of Revenue (Bureau) claims that the contractors are subject to these taxes because they are not the agents of the government but are instead independent contractors who are reimbursed for the performance of services under their contracts with ERDA, the costs of which include employees salaries, suppliers', subcontractors' and other costs of engaging in business in New Mexico. The State further claims that the United States has no right to be a party to the administrative tax proceedings because it is not the "taxpayer" under Section 72-13-15(0), N.M.S.A. 1975 Supp.

The resolution of the plaintiff's first claim depends upon whether the tangible personal property is sold to the contractor, or to the United States or its agents. A vendor's receipts from sale to the United States or its agents are non-taxable under the New Mexico Gross Receipts and Compensating Tax Act. Sections 72-16A-1 to 72-16A-19, N.M.S.A. 1975 Supp. The United States is claiming to be the party to whom the property is sold through its procurement agents, Sandia and Zia, and seeks to invoke the deduction provision of Section 72-16A-14.9 which provides in part:

> Receipts from selling tangible personal property . . . to the United States or any agency or instrumentality thereof or the State of New Mexico or any political subdivision thereof may be deducted from gross receipts.

The Bureau has refused to authorize the issuance of appropriate nontaxable transaction certificates to these contractors on the basis that they are not the agents or instrumentalities of the United States and therefore any sales of tangible personal property to them are not sales to the United States.

An analysis of the contractual relationship between the United States and the contractors will establish to whom the tangible personal property is sold.

Sandia is a special subsidiary of Western Electric Company, Inc. and operator, since 1949, of the Government-owned Sandia Laboratories; Sandia was created and exists exclusively to perform Government research and development. It receives no fee or profit, owns no property except $1,000 in Government bonds constituting its nominal paid-in capital, and does not perform any private work.

Zia has been performing, since 1946, management, operational, maintenance, architect-engineer, procurement, and related work which facilitates ERDA research and development functions at the Los Alamos Scientific Laboratory. Although Zia owns property and performs separate private work, none of its property is involved in performance of the ERDA contract, and Zia keeps a distinct set of records which are owned by and maintained for the Government, and relate to the performance of the ERDA contract. In addition, all private work is performed by different employees in separate sections of the company away from Los Alamos.

LACI is devoted exclusively to the performance of construction work in support of the Los Alamos Scientific Laboratory, a wholly-owned government research and development facility. LACI is a separate corporation managed by Zia, and owns no tangible personal property. Zia procures all tangible personal property needed in per-

formance of the LACI-ERDA contract; LACI makes no purchases. Both Sandia and Zia procure property needed for contract performance by issuing purchase orders or purchase contracts to sellers.

Zia and LACI are paid fixed fees annually for work performed under their contracts with ERDA. Gross receipts taxes have been paid each year by Zia and LACI on these fixed fees, as compensation received for services rendered.

The ERDA management contracts involved in this case provide that title to all tangible personal property passes directly to the Government from the vendor; the contractors are not considered "owners" of any tangible personal property procured by them. Some tangible personal property is obtained directly from government sources, title to which is vested in the Government. The contracts also place the risk of loss of property acquired under the contracts upon the Government and provide for Government control over the disposition of the property and approval of property management procedures employed by each contractor.

The tangible personal property procured by the contractors and all other operational costs such as salaries, are paid for by the use of an "advanced funding" arrangement whereby funds are deposited into government bank accounts by way of letters of credit, and payments are made from these government funds by the issuance of drafts drawn by the contractors on the accounts. The Bureau claims that these funds are paid to the contractors as reimbursement for their own costs, and as compensation for services rendered. A review of the funding arrangements, agreements with the banks which provide for Government ownership of the funds in the accounts and control over the disposition thereof, and the liability provisions in the contracts which recognize the Government's obligation to pay all operational costs, indicates that no contractor funds are used to pay for contract costs. Instead, the contractors are empowered to pledge the credit of the Government. Obligations that are "properly in-

curred" by the contractors (that is, without willful misconduct or bad faith on the part of the contractors) are considered to be ERDA liabilities. If the Government failed to provide funding, the contractors would be excused from performance of the contracts, and the Government would be liable for all properly incurred and reported claims. The advanced funding scheme is not a system by which the contractors are reimbursed for their direct costs under the contract.

The contractual relationship of the contractors and the Government in this case is not the same as the typical cost-plus-fixed-fee contractor, such as the one in *Alabama* v. *King & Boozer*, 314 U.S. 1, 62 S.Ct. 43, 86 L.Ed. 3 (1949), who was obligated to pay its costs from its own funds, and was directly liable to obligees and was subsequently reimbursed by the Government. The facts in *King & Boozer*, supra, make it clear that no agency relationship existed.

Recognizing the constitutional prohibition against state taxation of the United States, *McCulloch* v. *Maryland*, 4 Wheat. 316, 4 L.Ed. 579, the Supreme Court in *Kern-Limerick, Inc.* v. *Scurlock*, 347 U.S. 110, 74 S. Ct. 403, 98 L.Ed. 546 (1954), held that a Government contractor may be exempt from or immune to taxes if the contractor is the agent of the United States. The same rationale is behind the New Mexico tax here in question, which exempts a vendor from paying gross receipts taxes on tangible personal property sold to the United States or its agents or instrumentalities. The contract in *Kern-Limerick* specifically named the contractor as the purchasing agent of the Government, and provided that the Government was directly liable to the vendors for obligations incurred by the contractor. For these reasons, the contractor was found to be the procurement agent of the United States and was thus exempt from the state taxes.

In determining whether the contractors in this case are the procurement agents of the Government, the surrounding facts and contract provisions must be analyzed. However, specific words naming the contractors as agents are not required, so long as it is clear from the contracts

and factual circumstances that the relationship is one of agency. *United States* v. *Livingston*, 179 F. Supp. 9 (E.D.S.C. 1959), aff'd per curiam, 364 U.S. 281, 80 S.Ct. 1611, 4 L.Ed.2d 1719 (1960); *United States* v. *Boyd*, 211 Tenn. 139, 363 S.W.2d 193 (1962).

Prior to July 1, 1977, the three contracts in this case did not use the word "agent" to define the relationship between the contractors and the Government, yet the method of operation and obligations set forth in those contracts would imply an agency relationship. The contracts were modified on July 1, 1977, during the course of this litigation; one of the reasons for this modification was to expressly recognize the "long standing agency status and authority" of the contractors "for certain purposes". Modification No. 30, Contract AT (29-1)-789, Supplemental Agreement. The Bureau recognized this agency relationship for a period of about twenty years before these modifications were made, during which time no taxes were claimed to be due on the advanced funds of the government as "gross receipts" of the contractors, nor on the revenue from sales of tangible personal property to these contractors. In 1967 the Bureau's position regarding the agency relationship of the contractors and the government changed, and this litigation ensued. The Bureau asserts that a federal agency may not legally modify a contract for the purpose of immunizing an otherwise-taxable entity from state taxes without Congressional authorization. This argument is disposed of by the conclusion that the Government and the contractors herein maintained an agency relationship for procurement purposes during the years of operation prior to the contract modifications, and have continued to do so to the present. They were not taxable before the modifications, because such modifications merely made the relationship more express, but did not change the agency relationship which had been in operation for three decades, and which had been recognized as such by the Bureau.

The Bureau argues that the purchase orders do not identify the contractors as the Government's agents, but instead, refer to them as "Buyers", and that the contrac-

tors are responsible for determining their needs, selecting buyers, negotiating price, and generally enjoying a great degree of responsibility and autonomy not normal to an agency relationship.

Just as the fact that title to tangible personal property passes directly from the vendor to the Government is insufficient in itself to establish an agency relationship, *Alabama* v. *King & Boozer*, supra, so too are the Bureau's arguments as set forth above insufficient to show the lack of such. *U.S.* v. *Bureau of Revenue*, 87 N.M. 164, 531 F.2d 212 (1975) (Hernandez, B.C. concurring). More important are the facts that these are management contracts, in existence for nearly thirty years, (not short term buyer-seller contracts) conducted in government-owned facilities, with government-owned funds, for the purpose of carrying out significant ERDA statutory responsibilities. The Government maintains control over the contractors' procurement systems, property management and disposal practices, method of payment of operational costs, and other operations under the contracts. In addition, the Government has the right of prior approval of all purchases above a certain amount as stated in the contracts. For these reasons and those discussed above, I conclude that Sandia and Zia are procurement agents of the United States and that any sales of tangible personal property to them are sales to the United States through its procurement agents, which are not subject to the 4% gross receipts tax imposed by the New Mexico Gross Receipts and Compensating Tax Act.

This determination is also dispositive of the question whether Sandia and Zia are liable for the compensating tax imposed on their purchases of tangible personal property in other states and brought into New Mexico for purposes of performing their contracts with ERDA. The New Mexico Court of Appeals recently held that "the legislature intended to make our gross receipts tax and our compensating tax correlate: an exemption from the gross receipts tax must also be treated as an exemption from the compensating tax." *Western Electric Company* v. *New*

Mexico Bureau of Revenue, 90 N.M. 164, 167, 561 P.2d 26, 29 (1976).

Although the state court's interpretation of its own taxing statute is not binding upon this court due to the federal question of Government immunity from state taxes, *First Agricultural National Bank* v. *Tax Commission*, 392 U.S. 339, 347, 88 S.Ct. 2173, 20 L.Ed.2d 1138 (1968), it is entitled to great weight and is conclusive if it is a reasonable interpretation in light of the operation of the statute. *American Oil Co.* v. *Neill*, 380 U.S. 451, 455–56, 85 S.Ct. 1130, 14 L.Ed.2d 1 (1965). There is nothing to indicate that the New Mexico court's interpretation noted above is anything but reasonable, especially in light of the purpose of the compensating tax, which is:

> . . . to protect New Mexico businessmen from the unfair competition that would otherwise result from the importation into the state of property without payment of a similar tax [as the gross receipts tax]. Section 72-16A-2 N.M. S.A. 1975 Supp.

Thus, the contractors are entitled to the deduction provision of the New Mexico Gross Receipts and Compensating Tax Act for purchases of tangible personal property both inside and outside New Mexico.

With regard to the Government's second claim, that the advanced funds are non-taxable under the New Mexico Gross Receipts Act, the language of the statute requires an analysis of whether these funds were "received" by the contractors, as compensation for services:

> 'gross receipts' means the total amount of money or the value of other consideration, received . . . from performing services in New Mexico . . . Section 72-16A-3(f) N.M.S.A. 1975 Supp.

The Bureau contends that the advanced funds are received by the contractor as payment for services not simply disbursed by the contractor as an agent to cover the cost of operations under the contracts.

The funds deposited in the special bank accounts by ERDA are the only monies available for payment of all of the contractor's operational costs. They are not to be dis-

bursed in any manner not consistent with contract performance; ERDA may exert direct control over the disbursement of the funds, and retains title thereto while they are on deposit with the bank. Zia and LACI receive a fixed fee as compensation for their services, upon which they pay gross receipt taxes; Sandia receives no fixed fee or profit. The Zia and LACI contracts prior to modification stated that "payment for allowable costs and of the fixed fee . . . shall constitute complete compensation for the contractor's services." Effective April 1, 1976, this language was modified as follows:

> As compensation for performance of work under this contract, the contractor shall be paid a fixed fee as hereinafter provided. Modification 66 to Zia contract, p. 12, and modification 56 to LACI contract, p. 12.

Judge Hernandez, in his special concurrence in *U.S. v. Bureau of Revenue*, supra, 87 N.M. at p. 168, 531 P.2d at p. 216, considered the language in the unmodified version of Zia and LACI's contract quoted above and found that it was meant "as merely a limitation upon the government's liability under the contract". Judge Hernandez held at p. 168, 531 P.2d at p. 216 that to construe it otherwise, in light of the contract as a whole, would be to unreasonably isolate certain words, and to strain their meaning "beyond ordinary or common usage". No other reasonable interpretation of this language is possible: the contract modifications simply clarify the intention of the parties and add support to the conclusion that the advanced funds are not meant to be compensation to the contractors.

Having found that these contractors are procurement agents of the United States, it follows that the funds which they use for operations are not received by them for services, but are funds which belong to the Government until they are used to pay operational costs. Therefore, the advanced funds are not "gross receipts" to the contractors, and they are not subject to the 4% gross receipts tax imposed by the New Mexico Gross Receipts and Compensating Tax Act.

With regard to the Government's third claim, it is clear from the foregoing that the United States is the real party

in interest and should be recognized as a party in any New Mexico administrative tax proceeding involving the three contractors involved herein or their vendors. The contracts here require the United States to pay all costs under the contracts including taxes. In *U.S.* v. *Bureau of Revenue*, supra, the New Mexico Court of Appeals held that this was sufficient to recognize the United States as a taxpayer under the statute and allow it to be a party in tax disputes with the Bureau. Similarly, federal cases have established that, in cases involving a challenge to state taxes as violating the Government's sovereign and constitutional rights, the United States must be permitted to participate as a party. *U.S.* v. *Bureau of Revenue*, 291 F.2d 677 (10th Cir. 1961); *Marquardt Corporation* v. *Weber County*, 360 F.2d 168 (10th Cir. 1966), expressly overruling *U.S.* v. *Bureau of Revenue*, 217 F.Supp. 849 (D.C.N.M. 1963) which held to the contrary.

Under the circumstances of this case, the United States is the "taxpayer" under Section 72-13-15(0), N.M.S.A. 1975 Supp. and must be given the opportunity to participate as a party in any administrative proceedings before the New Mexico Commissioner of Revenue involving the tax liabilities of Zia, Sandia, LACI or their vendors.

A declaratory judgment will be entered consistent with this opinion.

APPENDIX B

United States Court of Appeals

FOR THE TENTH CIRCUIT

No. 78-1755

UNITED STATES OF AMERICA, PLAINTIFF-APPELLEE

v.

STATE OF NEW MEXICO; BUREAU OF REVENUE OF THE STATE OF NEW MEXICO; AND FRED L. O'CHESKEY, AS COMMISSIONER OF REVENUE OF THE STATE OF NEW MEXICO AND HIS SUCCESSORS IN OFFICE, DEFENDANTS-APPELLANTS

ON APPEAL FROM THE UNITED STATES DISTRICT COURT FOR THE DISTRICT OF NEW MEXICO

Decided and Filed June 2, 1980

Before: McWILLIAMS, BARRETT AND McKAY, *Circuit Judges*

McKAY, *Circuit Judge*. The United States seeks a declaratory judgment defining the status for purposes of the New Mexico Gross Receipts and compensating Tax[1] of

[1] When this suit was instituted, the tax was codified at N.M. Stat. Ann. §§72-16A-1 through 72-16A-19 (Supp. 1975). The tax has since been amended and now constitutes N.M. Stat. Ann. §§7-9-1 through 7-9-81 (1978). Citations in this opinion conform to the earlier enumeration. We refer only to the gross receipts tax because a determination of liability or exemption under the gross receipts tax will apply as well to the compensation tax. *See Western Elec. Co.* v. *New Mexico Bureau of Revenue*, 90 N.M. 164, 169, 561 P. 2d 26, 29 (1976).

three private corporations under management contracts with the Energy Research and Development Administration (ERDA), the successor to the Atomic Energy Commission (AEC).[2] The government also seeks a declaration that, as a matter of constitutional law, it must be permitted to intervene in any New Mexico administrative proceeding involving the tax status of the three corporations.

The government's substantive arguments focus on whether the contractors are agents of the United States for certain functions.[3] As agents for the disbursement of federal funds, they would be constitutionally immune from application of the gross receipts tax to those funds.[4] *See*

[2] Initially, research and development for nuclear weapons was the responsibility of the Army Corps of Engineers. Responsibility was subsequently transferred to the AEC (January 1, 1947), the ERDA (January 19, 1975), and finally the Department of Energy (October 1, 1977). *See* Department of Energy Organization Act, 42 U.S.C. §§7101 *et seq.*

[3] Other potential issues were resolved by a companion case in this court and a prior action between these parties in a state court. In *United States* v. *New Mexico*, 581 F.2d 803 (10th Cir. 1978), we determined the incidence of the gross receipts tax. In *United States* v. *Bureau of Revenue*, 87 N.M. 164, 531 P. 2d 212 (Ct.App. 1975), the New Mexico Court of Appeals held that the state was estopped from collecting assessments from two of the contractors for the period January 1, 1966, to June 30, 1967. The Bureau of Revenue had previously considered the contractors to be agents and had not given notice of its change of position. Lack of sufficient notice is not an obstacle to this suit. We note also that the Bureau's prior understanding of agency law in no way requires that a federal court find an agency relationship to exist now. For purposes of intergovernmental immunity, the applicable agency law is necessarily federal. New Mexico quite properly could change its own definition of agency so long as its new definition did not impinge on the area of immunity mandated by the Constitution.

[4] Although Congress could immunize these contractors from state taxation, it has not done so directly and congressional immunity will not be implied. *See Oklahoma Tax Comm'n* v. *Texas Co.*, 336 U.S. 342, 365-66 (1949). The contractors may nonetheless make a claim to constitutional immunity if their connection to the government is so close that a tax on them is in reality on the government. *See Alabama*

N.M. Stat. Ann. §72-16A-12.1 (Supp. 1975) (exemption for the government); N.M. Stat. Ann. §72-16A-3F (Supp. 1975) (requirement of receipt). In addition, if the contractors are procurement agents for the government, their suppliers of tangible personal property would be entitled to a tax deduction. *See* N.M. Stat. Ann. §72-16A-14.9 (Supp. 1975).

The parties filed cross-motions for summary judgment. Most facts, including the applicable contract language, were stipulated. The district court granted the motion of the United States, finding that the contractors were disbursement and procurement agents for the government and that the United States must be permitted to intervene in the state proceedings. The district court found that in paying their own operational costs—such expenses as overhead and salaries—the contractors were merely disbursing, not receiving, federal funds. The court also found that purchases of tangible personal property, even though used in the contractors' own work, were made as agents of the government.

We agree with the district court that the United States may intervene in state proceedings. However, we believe that the law which has developed to resolve agency questions in the government contract context requires that the district court grant summary judgment to New Mexico on the agency issues.

The three contracts involved here are in most respects standard AEC management contracts—a genre of contracts developed to facilitate the AEC's heavy reliance on private industry in the construction and management of large research and development facilities. Although AEC management contracts closely resemble typical cost-plus government contracts, they also contain unusual features. For instance, they contemplate long-term relationships and vest substantial autonomy in the contractors. *See* Hiestand & Florsheim, *The AEC Management Contract Concept*, 29 Fed. B.J. 67, 68 (1969).

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v. *King & Boozer*, 314 U.S. 1, 13 (1941); *McCulloch* v. *Maryland*, 17 U.S. (4 Wheat.) 316 (1819).

Under its contract, Sandia Corporation, a subsidiary of Western Electric Company, Inc., operates the Sandia Laboratories owned by ERDA. Sandia was created in 1949 to perform research and development for AEC, and it is not involved in private work. It receives no fee or profit under its contract and owns no property except the $1,000 in United States bonds constituting its nominal paid-in capital.

The Zia Company, a subsidiary of Santa Fe Industries, Inc., has been performing a variety of functions in support of ERDA's Los Alamos Scientific Laboratory since 1946. Zia performs separate private work with a distinct set of records, employees and locations. Virtually none of Zia's private property is involved in performance of its contract with ERDA.

Los Alamos Constructors, Inc. (LACI) is a subsidiary of the Zia Company. It performs construction work in support of the Los Alamos Scientific Laboratory. LACI owns no tangible personal property and procures the property needed in performance of its Los Alamos contract through Zia.

I.

The cornerstone case on whether a government contractor may share in the intergovernmental tax immunity enjoyed by the United States is *Alabama* v. *King & Boozer*, 314 U.S. 1 (1941). There the Supreme Court upheld a sales tax levied on the purchases of cost-plus-fixed-fee contractors notwithstanding the fact that the government would ultimately pay the tax in reimbursing the contractors' costs. The Court rejected an economic impact test and decided the case on the basis of the bare legal incidence of the tax. "The asserted right of the one [sovereign] to be free of taxation by the other does not spell immunity from paying the added costs, attributable to the taxation of [its contractors]." *Id.* at 9. The incidence of the tax was found to fall on the contractor, not the government, even though, *inter alia*, the government maintained extensive control over the contractor, the title to the goods pur-

chased subject to the tax passed directly to the government, and the government was to assume good faith obligations of the contractor upon termination of the contract.

In 1952 the Supreme Court interpreted §9(b) of the Atomic Energy Act of 1946 to be a legislative extension of governmental immunity to AEC contractors. *Carson* v. *Roane-Anderson Co.*, 342 U.S. 232 (1952). Congress promptly repealed §9(b), Act of August 13, 1953, Pub. L. No. 83-262, 67 Stat. 575 (1953), for the express purpose of putting AEC contractors on the same footing as other government contractors, who, since the decision in *King & Boozer*, are rarely found to be immune from taxation. The Senate Report accompanying the repealer discloses a congressional sensitivity to the decreased tax bases of those states with large-scale AEC activities. S. Rep. No. 694, 83rd Cong., 1st Sess., *reprinted in* [1953] U.S. Code Cong. & Ad. News 2379, 2380.

Since the decision in *King & Boozer*, the Supreme Court has only twice been satisfied that a sufficient relationship existed between the contractor and the government to qualify the contractor for implied constitutional immunity. In *Kern-Limerick, Inc.* v. *Scurlock*, 347 U.S. 110 (1954), the Court found a contractor to be an agent for the government for procurement and, therefore, immune from a sales tax. Language in the request for bids, the contract, and the purchase order clearly and uniformly disclosed an intention for the government to be directly obligated to the vendor for the contractor's purchases. *Id.* at 119-20. In the course of the opinion, the Court also noted the careful attention Congress has given to the proper adjustment of intergovernmental tax burdens. *Id.* at 116.

Justice Douglas, in his *Kern-Limerick* dissent, criticized the majority opinion insofar as it could be read to allow "any government functionary to draw the constitutional line by changing a few words in a contract." 347 U.S. at 126 (Douglas, J., dissenting). This concern—that immunity questions not turn on technicalities of contract drafting—reappeared in the majority opinions of the Michigan property cases decided four years later:

> Constitutional immunity from state taxation does not rest on such insubstantial formalities as whether the party using government property is formally designated a "lessee." *Otherwise immunity could be conferred by a simple stroke of the draftman's pen.*

United States v. *Township of Muskegon*, 355 U.S. 484, 486 (1958) (emphasis added). The Michigan opinions recognize Congress as "the proper agency . . . to make the difficult policy decisions necessarily involved in determining whether and to what extent private parties who do business with the Government should be given immunity from state taxes." *City of Detroit* v. *Murray Corp.*, 355 U.S. 489, 495 (1958). See also *United States* v. *City of Detroit*, 355 U.S. 466, 474 (1958). *Cf. United States* v. *Boyd*, 378 U.S. 39, 51 (1964).

In 1960 the Supreme Court affirmed, without opinion or citation, a three-judge district court determination that an AEC contractor in South Carolina was a tax-exempt government agent. *Livingston* v. *United States*, 364 U.S. 281 (1960) (per curiam), *aff'g* 179 F. Supp. 9 (E.D.S.C. 1959). The district court relied heavily on the fact that this AEC contractor undertook government work as a contribution to the defense effort rather than as a source of profit. Although the contract involved in *Livington* was typical of AEC management contracts in most respects, it provided for only a nominal one-dollar fee, and purchase orders were made on behalf of the government. 179 F. Supp. at 18. Later, in *United States* v. *Boyd*, 378 U.S. 39 (1964), the Supreme Court, considering another AEC management contract, sharply limited *Livingston* to the "'extraordinary' contractual relationship" involved and the "factual determination that [the contractor] received no benefits from the contract." *Id.* at 45 n.6.

In *Boyd*, the latest pertinent Supreme Court pronouncement, two AEC management contractors claimed exemption from a Tennessee use tax. After reviewing the contractual relationships involved, the Court affirmed the state supreme court determination that, despite extensive entanglement with the AEC, the incidence of the tax fell on the contractors' "private use" of government property

for their "own profit and gain." *Id.* at 43. The Court rejected the government's argument that the contractors were agents with the observation that they were not "constituent parts" or "instrumentalities" of the government. *id.* at 46–48. The opinion concluded by reserving to Congress the responsibility for readjustment if the Court's restricted interpretation of governmental immunity proves unworkable. *Id.* at 51.

Although there is language in these Supreme Court opinions suggesting that the results turn on traditional agency principles, *see e.g., United States* v. *Township of Muskegon*, 355 U.S. at 486, it seems evident that the Court is more concerned with preserving the delicate financial balance between our co-existing sovereignties than with rigid adherence to agency law terminology. The trend toward restricting tax immunities, *see generally* Powell, *The Waning of Intergovernmental Tax Immunities*, 58 Harv. L. Rev. 633 (1945), reflects an awareness of the serious threat posed to state revenues by ballooning governmental dealings in the private sector. *See* Note, *Federal Tax Immunity and the Legal Incidence of the Maine Sales Tax*, 29 Maine L. Rev. 149, 153–54 (1977). The Court has repeatedly deferred to Congress in this area and Congress, openly sensitive to the impact on state treasuries, has not extended tax immunity to any class of contractors.

We, too, are mindful of the tension between the power of the federal government to insulate itself from state tax burdens and the limited tax bases of state and local units. Clearly, Congress may legislatively provide tax immunity to federal contractors. In addition, under *Kern-Limerick* a federal agency may bring a contractor within the scope of intergovernmental immunity if a decision to create an agency relationship is made in advance of a dispute and is unequivocably expressed in all relevant documents.[5] The state may not similarily protect its treasury.

[5] It has been argued that tax immunity may be conferred only by the legislative branch. See L. Tribe, *American Constitutional Law* 399–401 (1978). This deference to Congress is amply supported by language

II.

With this concern for proper intergovernmental adjustments in mind, we have reviewed the assertions of each party. We dispose initially of the government's claim that the contractors do not receive, as required by the statute, see N.M. Stat. Ann. §72-16A-3F (Supp. 1975), the funds they disburse for their own salaries and overhead. As long as the contractors are separate entities solely responsible for their own employees and internal management, salaries and overhead cannot be the "obligations of another."[6] *Cf. Westland Corp.* v. *Commissioner of Rev-*

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in leading cases. See, e.g., *United States* v. *Boyd*, 378 U.S. 39, 51 (1964); *City of Detroit* v. *Murray Corp.*, 355 U.S. 489, 495 (1958). We agree that Congress is best able to adjust tax burdens, but we cannot ignore the power given to executive agencies to create relationships through contract. Although we are skeptical of cosmetic provisions drafted by government functionaries, we must find immunity when these contracts inherently and inexorably draw a private corporation so close to the government as to make it a servant. *See United States* v. *Forst*, 442 F. Supp. 920, 924-25 (W.D. Va. 1977), *aff'd*, 569 F.2d 811 (4th Cir. 1978).

[6]There is no deduction for expenses incurred in performing the service. *See* N.M. Stat. Ann. §72-16A-3K (Supp. 1975). Cf. *City of Los Angeles* v. *Clinton Merchandising Corp.*, 58 Cal.2d 675, 375 P.2d 851, 855 (1962). The statute is measured on gross rather than net proceeds; it taxes the privilege of conducting business in New Mexico, whether profitable or not. *See* N.M. Stat. Ann. §72-16A-2 (Supp. 1975). The failure of the legislature to reenact the predecessor statute's specific language prohibiting deduction for losses or expenses, *see* N.M. Stat. Ann. §72-16-2D (1953) (Emergency School Tax Act), does not alter the obvious meaning of the statute.

The government insists that Sandia, Zia and LACI are meeting the obligations of the government in paying salaries and fringe benefits, but that contractor employees have no claim against the government for labor-related grievances. *See* Record App. at 342. In other words, employees may not bargain with the government for the salaries and benefits supposedly flowing directly from the government. Acknowledging that tort liability depends on the "overall relationship between the United States and the contractor and on the control inherent in that relationship," Brief for Appellee at 48, the government nonetheless denies any tort responsibility for contractor negligence. Record App. at 342. As admitted, Sandia, Zia and LACI are not agents for the purpose of "directing the details of day-to-day research or maintenance

enue, 83 N.M. 29, 487 P.2d 1099, 1104 (Ct. App.), *cert. denied*, 83 N.M. 22, 487 P.2d 1092 (1971). The contractors are paying their own obligations and, regardless of the funding device employed, they receive the funds when they exercise dominion over them by issuing drafts to their obligees. To the extent that third parties are involved, in the procurement of goods and services for instance, it is possible that the contractors do function in an agency capacity and should, therefore, be tax exempt.

The factors urged as indicative of agency status here are not new to government contract cases. The contracts discussed in *United States* v. *Forst*, 442 F. Supp. 920 (W.D. Va. 1977), *aff'd*, 569 F.2d 811 (4th Cir. 1978), for example, contained several of the elements present here. Although the government conceded that the contractors in *Forst* were not agents, the court still analyzed the contractual characteristics necessary to make a contractor tax exempt. The court was unimpressed with the fact that all contract work was done at a government facility, 442 F. Supp. at 921, and that the government bore the risk of loss. *Id.* at 925. In addition, the court held that "it is not critical who holds the title to the purchased items as between the United States and its contractor. Nor is the degree of control over the contractor . . . critical." *Id.* at 924. See also *United States* v. *Township of Muskegon*, 355 U.S. 484 (1958). In affirming *Forst* the Fourth Circuit agreed that "the key factor in the case was whether the credit of the United States or the contractor was bound by the purchasing agreements." 569 F.2d at 811.

The argument that the contracts with Sandia, Zia and LACI inherently created agent-principal relationships is also at odds with the contracts discussed in *United States* v. *New Mexico*, 581 F.2d 803 (10th Cir. 1978). The contracts there specifically stated that the contractors were not agents but independent contractors. Ironically, those

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operations and the hiring and direct supervision of employees," Record App. at 33, but apparently only for the purpose of avoiding state taxation.

contracts were in most other respects very similar to the contracts we consider here. They provided, among other things, for the title of procured goods to pass directly to the government and for government approval of purchases over a stated amount. 581 F.2d at 804, 805.

An agency argument based on all the same factors present here was raised before the Supreme Court in *Boyd*.[7] *See* 378 U.S. at 46. The *Boyd* contractors, like Sandia, Zia and LACI, worked at a government facility with government property. They operated according to broad instructions from the AEC and obtained approval for purchases

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[7]The government challenges the applicability of *Boyd*. Concededly, *Boyd* does not decide the precise issue here but it provides us with an analogous situation in which similar considerations were weighed. In the Tennessee Supreme Court, *Boyd* focused on two questions: the imposition of state sales tax on the contractors' purchases and the imposition of a use tax on the contractor's use of AEC-owned property. *United States* v. *Boyd*, 211 Tenn. 139, 363 S.W.2d 193 (1962). The Tennessee court first found that the contractors were agents in purchasing for the AEC and therefore immune. On the second question the court concluded that, because the contractors used the property for their own benefit, the use tax was valid. Only the second finding was appealed. The United States Supreme Court noted specifically that it was not presented with the first issue and that "the validity of the contractor's use tax, as against a constitutional claim of immunity, in no way depends on the legality of the sales tax." *United States* v. *Boyd*, 378 U.S. 39, 43 n.5 (1964). We read this footnote neither as an approval of the state court's treatment of the issue not appealed, nor as a limit on the application of the Court's opinion to cases resembling the first issue. The Court merely noted that the two aspects of the taxing statute could be independently considered.

Because an agency issue was raised in *Boyd*, the applicability of the case turns on whether the taxed activity in *Boyd* is entirely distinguishable from the activities Sandia, Zia and LACI allegedly perform as agents. We think not. Using government property in the course of performing a government contract is not unlike incurring obligations to achieve the same end. If advanced funding is, as we believe, another form of reimbursement, the government has no different interest in a cost-type contractor's process of incurring and paying obligations than in any other function necessary to reach the desired result. Unless contract provisions provide otherwise, the government's interest dominates only in the result sought to be obtained by contract—here, research and development. *See* note, 13, *infra*.

above a stated figure. Title to property procured by the contractors passed directly to the government, which also bore the risk of loss. They also used advanced funding. The Court, in dismissing the agency claim, applied what may be even more stringent standards than we apply here. It found that the contractors were not "so assimilated by the Government as to become one of its constituent parts," 378 U.S. at 47 (quoting *United States* v. *Township of Muskegon*, 355 U.S. at 486), nor "so incorporated into the government structure as to become instrumentalities of the United States and thus enjoy governmental immunity." 378 U.S. at 43. This instrumentality language parallels the Atomic Energy Act which defines "Government agency" to include only those independent establishments or corporations which are wholly or partly owned by the government and which are also instrumentalities. 42 U.S.C. §2014(1). The government concedes that Sandia, Zia and LACI are not instrumentalities. Record App. at 345.

A number of other contractual features have been brought to our attention, but we find them either insubstantial or so common to government contracts generally that they have no particular bearing on the issue of agency. Characteristics common to virtually all AEC management contracts, even through not found in the contracts of other agencies, also have little impact on our determination. The repeal of §9(b) of the Atomic Energy Act illustrates congressional aversion to the notion that AEC contractors as a group are more entitled to tax immunity than are other federal contractors. Our reiterated antipathy to wholesale deprivations of state treasuries without congressional action, requires, at the least, some special arrangement before tax immunity attaches.

The government places emphasis on the fact that Sandia, Zia and LACI receive "advanced funding" from the ERDA rather than reimbursement for expenses. The contractors pay their creditors and employees with drafts drawn on a special bank account in which United States Treasury funds are deposited, under the authority of a let-

ter of credit, to cover withdrawals.[8] While the court in *Boyd* was no more impressed with the advanced funding aspect of the contracts it reviewed than with any other features, we find it worthy of discussion. On the surface advanced funding does appear to give the contractor the power to pledge the credit of the government—a significant indicator of agency status. *See Alabama* v. *King & Boozer*, 314 U.S. at 13-14; *United States* v. *Forst*, 442 F. Supp. 920, 925 (W.D. Va. 1977), aff'd, 569 F.2d 811, 811 (4th Cir. 1978).

Despite appearances, however, advanced funding does not create in the contractor the power to create obligations of the government as an agent.[9] At most, the con-

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[8]The steps involved in advanced funding are: (1) The contractor, the United States, and a designated bank open a special bank account pursuant to a three-party contract. The United States owns any balance in the account, but the contractor is given the right to execute drafts payable to third parties in order to satisfy any expenses incurred in performing the underlying government contract, *see* Record App. at 206-07, 209-18; (2) ERDA issues a letter of credit to an appropriate Federal Reserve Bank in favor of the contractor; this letter of credit provides the general authority for this Federal Reserve Bank to make United States Treasury funds available for deposit in the special bank account, *see* Record App. at 206-07, 220-21, 223, 224; (3) when a contractor incurs a contract expense, the contractor pays the expense by executing a draft payable to the creditor and drawn on the special bank account, *see* Record App. at 206-07; (4) at the time the contractor executes a draft on the special bank account, the contractor or the bank executes a payment voucher in an amount sufficient to cover the draft. This voucher is forwarded to the appropriate Federal Reserve Bank. The Federal Reserve Bank in turn deposits an equivalent sum to the account of the designated bank of deposit, and the designated bank of deposit credits the special bank account with funds sufficient to cover the draft. *See* Record App. at 205-08-, 219-22.

[9]The government asserts that it considers obligations properly incurred by Sandia, Zia and LACI to be obligations of ERDA. *See* Brief for Appellee at 35; Record App. at 207, 168, 173-74, 179, 338, 383. It is clear from the record, however, that this assertion is founded on the government's view of the ramifications of advanced funding and the fact that ERDA would not deny a valid claim arising from contract performance in the absence of sufficient advanced funds. *See* Record App. at 369-71. We are not bound by the government's assertion of

tractor may pledge to the limits of its letter of credit. Seen in this light, Sandia, Zia and LACI are like numerous businesses which deal under letters of credit from banks and other sureties. In fact, the federal government finances many organizations through letters of credit and advanced funding for which no claim of agency relationship could seriously be made. *See, e.g.*, Record App. at 237–42. Federal regulations allow letters of credit to be issued to "any State and local government educational institution, international organization and any other public and private organization." 31 C.F.R. §205.3(a). Like guarantees, advanced payment from customers does not transform independent contractors into agents.

Advanced funding is simply another means of reimbursement devised by accountants to eliminate major weaknesses in the government's bookkeeping practices:

> [Government agencies'] general practice when operating through private contractors on a reimbursable-cost basis, has been to record the initial sums paid such contractors as advances and to reflect costs in the Government's accounts only when contractors' expenditures have been audited and reimbursed by the Government. This practice has two basic weaknesses in the accounting . . .:
>
> (1) A considerable lag in time exists between the dates when the contractor incurs costs and when the Government accounts record the expenditures.
>
> (2) It is extremely difficult for the Government to break down the records of these expenditures so as to obtain a useful cost analysis . . . .

Fifth Semiannual Report of the Atomic Energy Commission 132 (1949), Record App. at 376. Advanced funding also encourages companies to undertake government con-

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direct liability because we believe advanced funding to be just another form of reimbursement, and ERDA responsibility for properly incurred claims to be inherent in all cost-type contracts. *See* 32 C.F.R. §7–402.2 (1976). The decision that cost reimbursement would not make government contractors into agents has been made for us. *See Alabama* v. *King & Boozer*, 314 U.S. 1 (1941).

tracts for little or no fee because it insulates contractors from the costs and risks of borrowing funds to meet contract obligations. Record App. at 208. Official documents make no distinction, other than for accounting purposes, between contractors which do or do not use advanced funding, *see* Ninth Semiannual Report of the Atomic Energy Commission 57–59 (1951), Record App. at 331–33, and we do not believe any distinction is warranted. As a matter of law, federal contractors are not transformed into tax-exempt agents by a federal agency's decision to change accounting practices or to simplify methods of payment.[10]

One of the contracts in this case requires particular consideration in light of *United States* v. *Livingston*, 179 F. Supp. 9 (E.D.S.C., 1959), *aff'd*, 364 U.S. 281 (1960). Sandia receives no fee for the performance of its contract with the government.[11] In *Livingston* a federal contractor was found to be a tax-exempt procurement agent because, among other things, its contract provided for only a one-dollar fee and was undertaken out of a "high sense of public responsibility" and "without hope of gain." 179 F. Supp. at 23, 18. Although we have doubts that such a factual determination would today withstand appellate review[12] we recognize the theoretical possibility that a "genuine issue of material fact" might be created on this

[10]The AEC had 43 contractors on advanced funding as of 1973. Ten were in New Mexico and 34 were private corporations. AEC Manual, Appendix 1101, Part III, §A at 5–6 (March 1973); Record App. at 388. As of 1977, 165 ERDA contractors had letters of credit and more than 8,000 are currently being issued to contractors by other federal agencies under general statutes and regulations authorizing advanced funding. *See* Record, Vol. 6, at 9 (McGrath depo.); 41 U.S.C., §255 (a)(1); 41 C.F.R. §§1–30.400 *et seq.* (1979); 31 C.F.R. §205.1–10 (1979).

[11]Zia and LACI receive fixed fees annually for work performed under their contracts with ERDA. Gross receipts taxes are paid on their fees. Record App. at 27. This challenge is limited to the funds used to pay their employees, suppliers and overhead.

[12]There are business advantages for ERDA contractors more valuable than a fee, for example, the acquisition of invaluable technical and engineering information and experience and the possibility of acquiring valuable patents as an outgrowth of research and development activities conducted at federal expense. Newman, *The Atomic Energy*

question. Nevertheless, we do not believe that this potential factual issue requires remand for a trial. The Supreme Court has limited *Livingston* not only to its peculiar "factual determination," but also to the "'extraordinary' contractual relationship" exhibited there. *United States* v. *Boyd*, 378 U.S. at 45 n.6. As we have indicated, the contracts here in issue are not extraordinary.

As with advanced funding, decisions on the amount of fee, if any, to be paid a government contractor are not made primarily with agency consequences in mind. The regulations provide for fee negotiations with each contractor, taking into account such factors as tax posture. *See* ERDA-PR Temporary Reg. No. 17, April 2, 1976, Record App. at 390–94. Without more, we decline to hang agency status, and thereby the welfare of state treasuries, on the existence or amount of a fee.

There is one final aspect of the contracts with Sandia, Zia and LACI which demands our attention. During the course of this litigation, the local ABC contracting officers in New Mexico modified these three contracts to refer directly to the contractors as agents, apparently in an attempt to fall within the shelter of *Kern-Limerick, Inc.* v. *Scurlock*, 347 U.S. 110 (1954), and to avoid New Mexico's argument that the omission of agency terminology was intentional. By their terms, however, the amendments add

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Industry: An Experiment in Hybridization, 60 Yale L.J. 1263, 1320–21 (1951). And while obtaining these benefits, Sandia is protected from usual business risks by advanced funding. Moreover, Sandia's profit-conscious parent, Western Electric, and its affiliates, *e.g.*, American Telephone & Telegraph Company, receive many benefits from Sandia's performance of the ERDA contract. They reserve nonexclusive, irrevocable, royalty-free licenses under any communication-related patents taken on discoveries made by Sandia. *See* Sandia Contract, Mod. No. 29, Art. IX, §1, Record App. at 142–43. The government pays Sandia's overhead and the salaries of parent-company employees who may be used or trained in the course of Sandia's operations. *See* Sandia Contract, Mod. No. 29, App. A, Art. III, §1, Record app. at 151. Through Sandia's contract, Western Electric and Bell Telephone Laboratories, Inc., are also paid for furnishing auditing services, research and development, products, and supervisory services. *See* Sandia Contract, Mod. No. 29, App. A, Art. III, §2-5, Record App. at 152–53.

nothing substantive to the contracts. To be sure, they state that the "contractor acts as an agent for and on behalf of ERDA for certain purposes." But they conclude with the caveat:

> The purpose of this article is to recognize and express existing relationships. This article shall not be construed to modify any other provisions of the contract . . . nor shall it create rights or obligations not otherwise provided for in the contract.

Zia Contract, Mod. No. M069, Record App. at 174. *See also* Sandia Contract, Mod. No. 30, Record App. at 169; LACI Contract, Mod. No. M059, Record App. at 179. Because we are convinced that, as a matter of law, the provisions of the contracts before the amendments did not establish agency status, we need not be swayed by amendments which make no changes.

It is also significant that the agency terminology does not appear uniformly in all the documents relating to the contracts. The "Standard Terms and Conditions accompanying their Purchase Orders" clearly distinguish between the "Buyer"—Sandia, Zia or LACI—and the "Government." Record App. at 247. Sandia's contract requires it to make purchase orders and subcontracts in its own name. Sandia Contract, Mod. No. 29, Art. XI, §2, Record App. at 145.

We are highly skeptical of the sporadic addition of "magic words" to a contract in an attempt to avoid state taxation. The importance of proper intergovernmental tax adjustments obligates us to require much more when the power to create agents is being exercised by the executive branch. While Congress may confer tax immunity in a word, an executive agency must clearly manifest the principal-agent relationship with all its ramifications if state taxation is to be precluded. There is not a clear manifestation here.

III.

On the final issue the district court determined that "the United States is the real party in interest and should be

recognized as a party in any New Mexico administrative tax proceeding involving the three contractors involved herein or their vendors." Record App. at 34. Our decision on the agency issues removes the rationale of the district court's determination. However, we are unwilling to conclude that the United States may properly be excluded, under all circumstances, from state tax proceedings involving these contractors.

Determination of the "real party in interest," as a matter of procedural fairness, should not be made in the absence of any possible relevant party. The United States must be permitted to intervene in the administrative proceedings to advocate on the facts its status as the real taxpayer. In fact, New Mexico courts and the Bureau of Revenue *have* permitted United States participation when "the contracts with Zia and LACI obligate the United States to provide funds necessary to defray all costs incurred in the performance of the contracts, including taxes." *United States* v. *Bureau of Revenue*, 87 N.M. 164, 531, P.2d 212, 213 (Ct. App. 1975). Participation is important in creating the full record necessary for appellate review should the Bureau deny the government's taxpayer claim. Finally, New Mexico provides us with no examples of prejudice that would result from United States participation. Cf. County of San Bernardino v. Harsh California Corp., 52 Cal. 2d 341, 340 P.2d 617, 621 (1959). Instead, the State admits its willingness to permit *de facto* government participation through representation of the contractors by the United States Attorney's office. Brief for Appellant at 60–61. Full participation by the United States would thus protect the United States without damaging any real interest of the state.

IV.

The district court should enter summary judgment in favor of New Mexico on the agency issues and the United States on the administrative proceeding issue:

1. Sales of tangible personal property to the ERDA, through its management contractors Sandia and Zia, are subject to the New Mexico gross receipt tax.

2. Advanced funds used for government operations under ERDA management contracts with Sandia, Zia and LACI are subject to the New Mexico gross receipts tax.

3. The United States has the right to participate in administrative tax proceedings wherein tax liabilities of Sandia, Zia and LACI are at issue.

APPENDIX C

In the United States Court of Appeals

FOR THE TENTH CIRCUIT

MAY TERM—JUNE 2, 1980

Before The Honorable ROBERT H. MCWILLIAMS, *Circuit Judge*, The Honorable JAMES E. BARRETT, *Circuit Judge*, and The Honorable MONROE G. MCKAY, *Circuit Judge*

UNITED STATES OF AMERICA, Plaintiff—Appellee,

vs.

STATE OF NEW MEXICO, BUREAU OF REVENUE OF THE STATE OF NEW MEXICO; AND FRED L. O'CHESKEY AS COMMISSIONER OF REVENUE OF AND FOR THE STATE OF NEW MEXICO, AND HIS SUCCESSORS IN OFFICE, DEFENDANTS—APPELLANTS

JUDGMENT

No. 78-1755
(D.C. No. 75-418-M)

This cause came on to be heard on the record on appeal from the United States District Court for the District of New Mexico, and was argued by counsel.

Upon consideration whereof, it is ordered that the judgment of that court is reversed in part and affirmed in part. The cause is remanded to the United States District Court for the District of New Mexico with instructions that it enter summary judgment in favor of New Mexico on the agency issues and in favor of the United States on the administrative proceeding issue:

1. Sales of tangible personal property to the ERDA, through its management contractors Sandia and Zia, are subject to the New Mexico gross receipts tax.

2. Advanced funds used for government operations under ERDA management contracts with Sandia, Zia and LACI are subject to the New Mexico gross receipts tax.

3. The United States has the right to participate in administrative tax proceedings wherein tax liabilities of Sandia, Zia and LACI are at issue.

/s/ Howard K. Phillips

HOWARD K. PHILLIPS
Clerk

APPENDIX D

N.M. Stat. Ann. 1953 (Supp. 1975):

§ 72-16A-3. *Definitions.*—As used in the Gross Receipts and Compensating Tax Act [72-16A-1 to 72-16A-19]:

* * * * *

B. "buying" or "selling" means any transfer of property for consideration or any performance of service for consideration;

* * * * *

E. "engaging in business" means carrying on or causing to be carried on any activity with the purpose of direct or indirect benefit;

F. "gross receipts" means the total amount of money or the value of other consideration, received from selling property in New Mexico, from leasing property employed in New Mexico or from performing services in New Mexico, and includes any receipts from sales of tangible personal property handled on consignment but excludes cash discounts allowed and taken, New Mexico gross receipts tax payable on transactions for the reporting period and taxes imposed pursuant to the provisions of the County Sales Tax Act [13-2-30 to 13-2-35], the County Gross Receipts Tax Act [15-55-1 to 15-55-15] or the Municipal Gross Receipts Tax Act [14-61-1 to 14-61-8] which are payable on transactions for the reporting period and any type of time-price differential.

In an exchange in which the money or other consideration received does not represent the value of the property or service exchanged, "gross receipts" means the reasonable value of the property or service exchanged.

* * * * *

"Gross receipts," for the purposes of the business of buying, selling or promoting the purchase, sale or leasing, as factor, agent or broker, on a commission or fee basis, of any property,

service, stock, bond or security, includes only the total commissions or fees derived from the business;

* * * * *

L. "use" or "using" includes use, consumption or storage other than storage for subsequent sale in the ordinary course of business or for use solely outside this state.

§ 72-16A-4. *Imposition and rate of tax—Denomination as "gross receipts tax."*—A. For the privilege of engaging in business, an excise tax equal to four per cent [4%] of gross receipts is imposed on any person engaging in business in New Mexico.

B. The tax imposed by this section shall be referred to as the "gross receipts tax."

§ 72-16A-7. *Imposition and rate of tax—Denomination as "compensating tax."* —A. For the privilege of using property in New Mexico, there is imposed on the person using property an excise tax equal to four per cent [4%] of the value, at the time of acquisition or of introduction into the state, whichever is later, or of conversion to use by the manufacturer of property that was:

(1) manufactured by the person using the property in the state;

(2) acquired outside this state as the result of a transaction that would have been subject to the gross receipts tax had it occurred within this state; or

(3) acquired as the result of a transaction which was not initially subject to the compensating tax imposed by subsection A(2) of this section of the gross receipts tax but which transaction, because of the buyer's subsequent use of the property, should have been subject to the compensating tax imposed by subsection A(2) of this section or the gross receipts tax.

B. For the privilege of using services rendered in New Mexico, there is imposed on the person using such services an excise tax equal to four per cent [4%] of the value of the services at the

time they were rendered. The services, to be taxable under this subsection, must have been rendered as the result of a transaction which was not initially subject to the gross receipts tax but which transaction, because of the buyer's subsequent use of the services, should have been subject to the gross receipts tax.

C. The tax imposed by this section shall be referred to as the "compensating tax."

* * * * *

§ 72-16A-12. *Exemptions.*—Exempted from the gross receipts or compensating tax are those receipts or uses exempted in sections 72-16A-12.1 through 72-16A-12.30 NMSA 1953.

§ 72-16A-12.1 *Exemption—Gross receipts tax—Governmental agencies.*—Exempted from the gross receipts tax are the receipts of the United States or any agency or instrumentality thereof or the state of New Mexico or any political subdivision thereof.

* * * * *

§ 72-16A-12.2. *Exemption—Compensating tax—Governmental agencies—Indians.*—Exempted from the compensating tax is the use of property by the United States or any agency or instrumentality thereof or the state of New Mexico or any political subdivision thereof.

* * * * *

§ 72-16A-14. *Deductions.*—In computing the gross receipts tax due, only those receipts specified in sections 72-16A-14.1 through 72-16A-14.32 NMSA 1953 may be deducted. Receipts, whether specified once or several times in sections 72-16A-14.1 through 72-16A-14.32 NMSA 1953, may be deducted only once from gross receipts.

* * * * *

§ 72-16A-14.9. *Deduction—Gross receipts tax—Sales to governmental agencies.*—Receipts from

selling tangible personal property, other than nonfissionable metalliferous mineral ore, to the United States or any agency or instrumentality thereof or the state of New Mexico or any political subdivision thereof may be deducted from gross receipts. Receipts from selling tangible personal property, other than nonfissionable metalliferous mineral ore, to the governing body of any Indian tribe or Indian pueblo for use on Indian reservations or pueblo grants, may be deducted from gross receipts.

* * * * *

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CLERK

No. 80-702

In the Supreme Court of the United States

OCTOBER TERM, 1980

UNITED STATES OF AMERICA,
Petitioner

v.

STATE OF NEW MEXICO, ET AL.

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE TENTH CIRCUIT

JOINT APPENDIX

PETITION FOR CERTIORARI FILED OCTOBER 30, 1980
CERTIORARI GRANTED FEBRUARY 23, 1981.

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UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF NEW MEXICO

No. 75-418

UNITED STATES OF AMERICA, PLAINTIFFS

v.

STATE OF NEW MEXICO; BUREAU OF REVENUE OF THE STATE OF NEW MEXICO; and O'CHESKEY, Presiding as Commissioner of Revenue of and for the State of New Mexico and his successors in office, DEFENDANTS

RELEVANT DOCKET ENTRIES

DATE	NR.	PROCEEDINGS
7-17-75	1	Complaint with attachments.
		Summons, original and three copies issued and with complaint attached thereto delivered to the Marshal for service.
	7	ANSWER by defts containing affirmative defenses.
1-5-76	9	MOTION by defts to dismiss complaint for absence of a case or controversy and of issues ripe for adjudication.
	10	MEMORANDUM in support of defts' motion to dismiss the complaint herein.
	11	AFFIDAVIT by Fred L. O'Cheskey.
1-29-76	12	OPPOSITION by pltf to defts' motion to dismiss complaint and opposition to defts' other procedural defenses raised in their answer.
	13	MEMORANDUM OF POINTS AND AUTHORITIES by pltf in support of their opposition to defts' motion to dismiss and other procedural defenses raised in their answer.

DATE	NR.	PROCEEDINGS
	14	REQUEST FOR ADMISSIONS by pltf.
	15	INTERROGATORIES by pltf to deft.
2-27-76	16	REPLIES TO INTERROGATORIES by defts.
	17	RESPONSE by defts to request for admissions.
3-29-76	18	MOTION by pltf for summary judgment.
	19	MEMORANDUM of points and authorities by pltf in support of motion for summary judgment with exhibits attached.
4-8-76	20	MOTION by defts to dismiss complaint for absence of standing on the part of pltf to bring this action.
	21	MEMORANDUM in support of deft's motion to dismiss for lack of standing.
6-11-76	25	ORDER that the motion of the defts to dismiss is denied. (MECHEM) Copies mailed to counsel.
7-6-76		SUPPLEMENTAL EXHIBITS by pltfs in support of its motion for summary judgment.
7-28-76	26	INTERROGATORIES by defts.
8-30-76	27	AFFIDAVIT of John F. McNett.
	28	ANSWERS TO INTERROGATORIES by pltf.
10-15-76	29	Pl's SUPPLEMENTAL ANSWERS to Defts' Interrogatories (First Set)
11-8-76		Set for PTC 11-17-76 at 9:00 A.M. at Albuq. Counsel notified.
11-17-76		Judge Mechem holds pretrial conference.
2-7-77	30	PLAINTIFF'S SUPPLEMENTAL ANSWERS to Defendants' Interrogatories. (Second Set) with Exhibits in Two Volumes.
3-25-77	31	SECOND SET OF SUPPLEMENTAL DOCUMENTS by pltf in support of its motion for summary judgment, with exhibits attached.

DATE	NR.	PROCEEDINGS
4-27-77	32	NOTICE TO TAKE DEPOSITION of Mr. Daniel McGrath by defts.
	33	REQUEST by defts to produce and permit inspection and copying documents.
6-22-77	34	REQUEST FOR PRODUCTION by defts.
6-22-77	35	SUPPLEMENTAL ANSWERS TO INTERROGATORIES by pltf.
7-12-77		Set for trial at Albuq. 8-1-77 at 9:00 A.M. Counsel notified.
7-22-77	36	RESPONSE by pltf to request for production.
	37	ANSWERS TO ADDITIONAL INTERROGATORIES 122, 123, & 124 by pltfs.
7-28-77	38	THIRD SET OF SUPPLEMENTAL DOCUMENTS by pltf in support of its motion for summary judgment.
8-3-77	39	REQUEST FOR PRODUCTION by defts.
8-10-77		DEPOSITION of Anthony G. Carretta and Daniel H. McGrath, Jr.
8-31-77	41	MOTION by defts to compel discovery,
	42	MEMORANDUM in support of motion to compel discovery.
9-1-77	43	CERTIFICATE by Daniel H. Friedman of compliance with local rule 10(c).
9-7-77	44	MEMORANDUM by pltf in opposition to defts' motion to compel discovery.
9-9-77	45	STIPULATION by parties as to certain facts.
9-15-77	46	AFFIDAVIT of John F. McNett.
3-22-77	47	STIPULATION by parties as to certain answers to interrogatories.

DATE	NR.	PROCEEDINGS
9-26-77	48	DEFT'S CROSS MOTION FOR SUMMARY JUDGMENT W/SUPPORTING MEMORANDUM AFFIDAVITS AND EXHIBITS.
10-6-77	50	OPPOSITION by pltf to defts' cross motion for summary judgment with exhibits attached.
10-17-77	51	MOTION by defts to exclude evidence.
	52	MEMORANDUM by defts in support of its motion to exclude evidence.
10-27-77	53	RESPONSE by pltf to motion to exclude evidence.
10-31-77	54	AFFIDAVIT of Daniel H. McGrath, Jr..
8-4-78	55	ORDER that the deft's motion to exclude evidence is denied. (MECHEM) Copies to counsel.
	56	MEMORANDUM OPINION. (MECHEM) Copies to counsel.
	57	DECLARATORY JUDGMENT THAT sales of tangible personal property to the Environmental Research and Development Administration are sales to the US through its procurement agents which are not subject to the 4% gross receipts tax nor to the compensating tax imposed by the NM Gross Receipts and Compensating Tax Act. (MECHEM) Copies to counsel.
		FINAL ENTRY
8-14-78		Memorandum Opinion mailed for publication.

UNITED STATES COURT OF APPEALS
FOR THE TENTH CIRCUIT

No. 78-1755

GENERAL DOCKET

DATE	PROCEEDINGS
—/18/78	Cause docketed, docketing statement, orig. & 9 cc, c/s.
—/30/79	HRG. SET Hearing set for October, 1979, Special Session—Denver, Colorado
10/16/79	CS.ARG.SUBM.—case argued and submitted to McWilliams, Barrett, McKay
6/2/80	OPN.F. Published, signed opinion filed—McWilliams, Barrett, McKay Writing Judge is McKay JM.DISP. Judgment affirmed in part, reversed in part. The cause is remanded.
6/10/80	OPN.RMK. Ordered page 10, line 5 of footnote 6—change the word "takes" to "taxes"—McWilliams, Barrett, McKay
6/24/80	MDT.ISS—mandate issued to district court
11/3/80	P.WRIT.CERT.F Appellant's filing of petition for writ of certiorari on October 30, 1980, Supreme Court #80-702.
2/26/81	P.WRIT.CERT.DISP. Appellant's petition for writ of cert granted by Supreme Court order filed 2/23/81.

IN THE UNITED STATES DISTRICT COURT
FOR THE
DISTRICT OF NEW MEXICO

Civil Action No. 75-418

Complaint (R.I-1)

UNITED STATES OF AMERICA, PLAINTIFF

v.

STATE OF NEW MEXICO;
BUREAU OF REVENUE OF THE STATE OF NEW MEXICO;
and FRED L. O'CHESKEY, as Commissioner of
Revenue of and for the State of New Mexico,
and his successors in office, DEFENDANTS

COMPLAINT

Comes now the plaintiff, United States of America, by its attorney, Victor R. Ortega, United States Attorney for the District of New Mexico, and complains and alleges as follows:

1. This is a civil action instituted by the United States of America for the purpose of obtaining from this Court a declaratory judgment ordering and adjudging that the Constitution and the laws of the United States and the laws of the State of New Mexico prohibit the imposition or application of certain provisions of the New Mexico Gross Receipts and Compensating Tax Act (Sections 72-16A-1 through 72-16A-19, N.M.S.A., 1953, as amended, effective July 1, 1967 hereinafter sometimes referred to as the "Tax Act") against certain activities performed by the United States through its federal contractors. Erroneous application of the Tax Act to said activities could illegally subject the plaintiff, United States of America, to liabilities exceeding ten million dollars ($10,000,000) per year.

2. This action has been authorized and requested by a delegate of the Energy Research and Development Administration (hereinafter referred to as "ERDA"), an independent agency of the United States of America established under the provisions of Public Law 93-438, and is brought under the direction of the Atorney General of the United States, to protect the pecuniary interests and sovereign rights of the United States.

3. Jurisdiction of this action is conferred upon this Court by the provisions of Sections 1345 and 2201 of Title 28, United States Code, for the reason that this is a civil action brought by the United States to obtain a declaratory judgment from this Court respecting the interests of the United States.

4. An actual controversy, as is more fully described below, has arisen and now exists between the United States of America and the defendants concerning their respective rights and duties and plaintiff is suffering actual and threatened harm by virtue of actions of the defendants.

5. Plaintiff, United States of America, is a corporate sovereign and body politic.

6. (A) The defendant, State of New Mexico, is a body politic and corporate sovereign and is joined as a defendant in this action because the action involves the interpretation of a State law and its application. (B) The defendant, Bureau of Revenue of the State of New Mexico, is the State agency responsible for the administration and enforcement of the New Mexico tax laws, including the New Mexico Gross Receipts and Compensating Tax Act. (C) Defendant, Fred L. O'Cheskey is the Commissioner of Revenue of and for the State of New Mexico and is joined herein in his official capacity.

7. In the performance of its governmental functions, plaintiff, United States of America, and more specifically, ERDA, has entered into, prior to and since enactment of the Tax Act, and will enter into contracts with, and

has employed, contractors to perform activities to further its governmental functions.

8. The United States owns the Los Alamos Scientific Laboratory at Los Alamos, New Mexico which is devoted exclusively to the conduct of research and development for the United States Government.

9. The Zia Company (hereinafter referred to as "Zia"), a corporation organized and existing under the laws of Delaware, has since April 1, 1946 been performing work for the United States as an operating contractor in support of Governmental operations at the Los Alamos Scientific Laboratory under an operating contract with ERDA. Zia performs management, operational, maintenance, architect-engineering, procurement and other related support activities for the United States at Los Alamos and is paid a fixed-fee negotiated annually. Zia pays New Mexico gross receipts taxes imposed by the Tax Act based on the amount of its fixed-fee.

10. Los Alamos Constructors Inc. (hereinafter referred to as "LACI"), a corporation organized and existing under the laws of New Mexico, has since March 31, 1953, been performing work for the United States as an operating contractor in support of Governmental operations at the Los Alamos Scientific Laboratory under an operating contract with ERDA. LACI performs construction, alteration, and repair work, and other related support activities for the United States at Los Alamos and is paid a fixed-fee negotiated annually. LACI pays New Mexico gross receipts taxes imposed by the Tax Act based on the amount of its fixed-fee.

11. Sandia Corporation (hereinafter referred to as "Sandia"), a corporation organized and existing under the laws of the State of Delaware has, since 1949, operated Sandia Laboratories, which are Government-owned facilities devoted exclusively to the conduct of research and development for the United States. The principal facilities of Sandia Laboratories are located in Albuquerque, New Mexico. Sandia is a subsidiary of Western Electric

Company (hereinafter referred to as "Western") a corporation organized and existing under the laws of the State of New York. Sandia was created for the sole purpose of operating the Government-owned Sandia Laboratories and performing research and development for the United States under an operating contract between ERDA and Western. Neither Sandia nor Western receives any fee or profit in any form for its activities under the operating contract.

12. It is provided, pursuant to ERDA operating contracts with Zia, LACI and Western, that the United States is obligated to pay directly from Government funds the costs of conducting Government activities, including legal taxes, and that pursuant to each of these ERDA operating contracts, ERDA establishes and maintains United States Government advanced funding, hereinafter described in more detail, through which payments are made for all purchases, expenditures, and costs incurred thereunder, resulting in the expenditure only of United States funds for the purchase of tangible personal property, services and other expenses under these ERDA operating contracts.

13. In order to facilitate Government operations, United States Government advanced funding is established and maintained for each ERDA operating contract by creating a United States Government account which is identified as a special account of the United States Energy Research and Development Administration. Under the ERDA contract, title and ownership of the special United States Government account and balance therein, if any, remains in the Government, and the ERDA operating contractor at no time acquires any right, title or interest in such United States Government account, other than the obligation to make Government expenditures therefrom as provided in the ERDA contract.

14. It is provided under the ERDA operating contracts, that title and ownership of all tangible personal property acquired for use under all operating contracts pass di-

rectly from the vendor to the Government and remain at all times in the Government and never at any time vest in any ERDA operating contractor.

15. In response to ERDA's letter of January 30, 1975 (attached hereto as "Exhibit 1"), the New Mexico Commissioner of Revenue as evidenced by his letter of February 28, 1975 to ERDA (attached hereto as "Exhibit 2"), has (a) refused to provide appropriate nontaxable transaction certificates to Zia and LACI and (b) has insisted that ERDA's operating contractors continue to maintain burdensome and costly record-keeping activities which would not be necessary if nontaxable transaction certificates were issued, and by doing so has harmed the plaintiff, United States of America. The Commissioner also threatens to assess gross receipts taxes against vendors from which ERDA procures its tangible personal property, through its operating contractors, under transactions in which title and ownership of the property pass directly from the vendors to the Government and payment to the vendors is made directly from special United States Government advanced fund accounts described in Paragraph 12 above, contrary to the provisions of the Constitution and laws of the United States and the Tax Act.

16. The New Mexico Bureau of Revenue and Commissioner of Revenue have assessed and now threaten to assess ERDA operating contractors, including Zia, LACI and Sandia gross receipts taxes on the basis of Government-owned advanced fund accounts maintained as described in Paragraph 12 above, contrary to the provisions of the Constitution and laws of the United States, and the Tax Act.

17. The New Mexico Bureau of Revenue and Commissioner of Revenue, have assessed and now threaten to assess compensating (use) taxes against ERDA contractors based on the use of Government-owned tangible personal property purchased pursuant to ERDA contracts with advanced funds as described above, contrary to the

provisions of the Constitution and laws of the United States and the Tax Act.

18. By refusing to issue nontaxable transaction certificates to United States ERDA operating contractors, by imposing a costly record-keeping burden on United States ERDA operating contractors, by refusing to recognize the principles of law as declared in the concurring opinion in the case of *United States, Zia and LACI* v. *Bureau of Revenue, State of New Mexico*, New Mexico Court of Appeals, No. 1217, January 8, 1975 (N.M.St.Bar Vul.V.13 #42 1975, pp. 558-562), and by threatening to assess such contractors for gross receipts taxes measured by United States Government advanced funds and assess compensating (use) taxes on property owned by the United States Government, the New Mexico Bureau of Revenue and Commissioner of Revenue have violated the Constitution and laws of the United States and the Tax Act.

19. The New Mexico Bureau of Revenue and Commissioner of Revenue, have denied and threaten to deny to the United States its right, as a matter of law, under the Constitution and laws of the United States and under the laws of the State of New Mexico to intervene in proceedings before the Bureau wherein the taxes in dispute must be or are paid by the United States pursuant to its contractual obligations.

20. Under terms of contracts between ERDA and its operating contractors, the United States Government is obligated to bear the burden of any taxes paid by Zia, LACI, or Sandia.

WHEREFORE, plaintiff, United States of America, prays that this Court enter an Order granting a declaratory judgment, ordering and adjudging, in light of the Constitution and laws of the United States and the laws of the State of New Mexico, including the Tax Act, that:

1. United States Government advanced funds are not taxable gross receipts to operating contractors of the

United States Energy Research and Development Administration;

2. the receipts of vendors from the sale of tangible personal property to the United States Energy Research and Development Administration, acting through its operating contractors, wherein title and ownership of such tangible personal property pass directly from the vendor to the United States Government and payment is made from United States Government advanced funds, are not taxable gross receipts;

3. United States Government-owned tangible personal property purchased by the United States Energy Research and Development Administration, through its operating contractors, with United States Government advanced funds is not subject to compensating (use) taxes;

4. the United States is entitled, as a matter of law, to intervene in administrative tax proceedings before the New Mexico Commissioner of Revenue wherein the taxes in dispute are paid or must be paid by the United States pursuant to its contractual obligations; and

6. such other and further relief as may be just and proper.

VICTOR R. ORTEGA
United States Attorney

By: _____

Of Counsel:

JOHN J. MCCARTHY, Chief
General Litigation Section
Tax Division

/s/ Charles E. Stratton
CHARLES E. STRATTON
Trial Attorney—Tax Division
U.S. Department of Justice
Washington, D.C. 20530
Telephone: (202) 739-3056

"EXHIBIT 1"

Jan. 30, 1975

Honorable Fred L. O'Cheskey
Commissioner of Revenue
State of New Mexico
Santa Fe, New Mexico 87501

Dear Mr. O'Cheskey:

In December of 1969 the Atomic Energy Commission entered into a written agreement (Contract AT(29-2)-2849) with Commissioner Franklin Jones for the issuance of special temporary nontaxable transaction certificates for use by our New Mexico operating contractors in purchasing tangible personal property for the Atomic Energy Commission. Since that date we have maintained records, as required by our agreement, to account for the taxes which would have been collected on those transactions.

With your concurrence we propose now to advise our contractors that the keeping of these records of contingent tax liabilities for current and past periods is no longer necessary in light of the January 8, 1975, decision of the New Mexico Court of Appeals in *United States of America, The Zia Company, and Los Alamos Constructors, Inc.* v. *Bureau of Revenue*, No. 1217. As you know, that decision holds that our operating contractor, The Zia Company, was not subject to compensating tax on its purchases of tangible personal property for the Atomic Energy Commission in accordance with rulings issued by your predecessors which, as specifically noted by the concurring opinion of Judge B. C. Hernandez, were correct interpretations of the applicable New Mexico and federal law.

We would also request that you now issue standard type 9 nontaxable transaction certificates for use by those contractors previously authorized to use special certificates

under the AEC-Bureau of Revenue agreement. These contractors are: The Zia Company, Sandia Corporation, Lovelace Foundation, and EG&G (Nevada Operations activity). The University of California, though originally covered by the agreement, is now using separate NTTC's as a 501(c)(3) organization pursuant to your authorization of May 18, 1973. We would be happy to provide you with current contract provisions, purchase orders, bank account agreements, or any other documentation you need to assure yourself that the other contractors fall within the scope of the *Zia* decision.

We believe that the issuance of permanent certificates at this time is in accordance with ruling 69-001-18, dated December 18, 1969. That ruling, signed by Commissioner Jones and Deputy Attorney General O'Dowd, provided:

> "If a court of competent jurisdiction issues a final decision, not subject to review, which holds that the taxes imposed by the New Mexico Gross Receipts and Compensating Tax Act, Sections 72-16A-1 et seq., N.M.S.A. 1953 Comp., do not apply to some or all of the transactions for which the buyers have executed Special Certificates the Bureau may withdraw the Special Certificates, in whole or in part, and may issue such standard nontaxable transaction certificates in their place as may be indicated by the court's decision. No gross receipts or compensating tax liability shall be imposed as a result of such withdrawal for any past or future transactions which are the subject matter of the court's decision."

The period of uncertainty concerning the tax status of our operating contractors in New Mexico has been of much longer duration that we anticipated in 1969. Each year since 1969 we have faced higher costs and tighter budgets for our operations in New Mexico. Under these circumstances we must take special care to eliminate wherever possible unnecessary administrative burdens. This objec-

tive is especially important today when we are in a critical period of transition from the Atomic Energy Commission to the Energy Research and Development Administration. Accounting for contingent tax liabilities is a particularly burdensome process which would now appear to be unnecessary. I would, therefore, appreciate hearing from you at an early date with regard to these matters.

If there is any way in which my staff or personnel of our operating contractors can be of assistance in bringing this matter to a conclusion, please do not hesitate to call upon us. In view of the importance of this matter to the new Energy Research and Development Administration, I would appreciate your directing your correspondence to me.

Sincerely,

/s/ H. C. Donnelly
H. C. DONNELLY
Manager

OGG:JFM

bcc: Charles E. Stratton, Esq.
General Litigation Section
Tax Division
U.S. Department of Justice
3313 Old Star Bldg.
Washington, D.C. 20530

Sally M. Gerety, Counsel, LAAO

"EXHIBIT 2"

[SEAL]

An Equal Opportunity Employer

STATE OF NEW MEXICO
BUREAU OF REVENUE
Santa Fe, New Mexico
87801

TO: John Cho, Asst. Counsel, H
ATTN: Brian Kildee, Attorney
Phone for pickup 4565

Feb. 28, 1975

Mr. H. C. Donnelly
Manager
U.S. Energy Research & Development
Administration
Albuquerque Operations Office
P.O. Box 5400
Albuquerque, New Mexico 87115

Dear Mr. Donnelly:

Your letter asks for my concurrence to your informing your contractors that records of contingent tax liabilities are no longer necessary.

The Court of Appeals' decision did not reach the substantive issue of tax liability of companies such as Zia. The only question decided by the majority was the matter of estoppel under the now repealed Emergency School Tax and Compensating Tax Act. Moreover, Judge Hernandez' opinion is not the law of the case.

Since the important issues raised are unresolved, it would be premature to advise these contractors who are addressees of Ruling 60-001-18 to abandon their record

keeping obligations. Nor does the Bureau propose to issue Type 9 Certificates at this time.

Previous agreements have prevented collection of great amounts of revenue by this state. This burden is certainly as great as the burden of record keeping on your contractors. Because the Court's opinion does not reach the ultimate issues, the Bureau is not prepared to concede these issues and we will have to present another case to the Court. Therefore, all parties now bound by the ruling must continue to bear their respective burdens until the courts finally address the important questions involved.

Very truly yours,

/s/ Fred L. O'Cheskey
FRED L. O'CHESKEY
Commissioner of Revenue

FLO'C/VOH/ca

EXCERPTS FROM ATOMIC ENERGY COMMISSION CONTRACT W-17-028-ENG-90 DATED JULY 1, 1970, WITH THE ZIA COMPANY (R. II)

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ARTICLE VI—ALLOWABLE COSTS AND FIXED FEE

1. *Compensation for Contractor's Services.* Payment for the allowable cost as hereinafter defined, and of the fixed fee, if any, as hereinafter provided, shall constitute full and complete compensation for the performance of the work under this contract. It is understood and agreed, however, that the fixed fee shall be allowed the Contractor only for those services which are performed by the Contractor under Section 1.a. of the article entitled "Statement of Work," and that no fee shall be allowed the Contractor by the Government for those services which are performed by the Contractor for Constructors under Section 1.b. of such article.

2. *Fixed Fee.* The fixed fee payable to the Contractor for the performance of the work under this contract for the period July 1, 1970, through June 30, 1971, is One Hundred Twenty Thousand Dollars ($120,000.00).

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ARTICLE VII——PAYMENTS AND ADVANCES

1. *Installments of Fixed Fee.* The fixed fee provided for in Article VI shall be paid in equal monthly installments as it accrues.

2. *Payments on Account of Allowable Cost.* The Contracting Officer and the Contractor shall agree as to the extent to which payment for allowable costs or

payments for other items specifically approved in writing by the Contracting Officer shall be made from advances of Government funds. The Contractor shall submit a separate voucher for each installment of the fixed fee as it accrues, and with the written approval of the Contracting Officer, may pay such installment of the fixed fee out of advances of Government funds.

3. *Special Bank Account—Use.* All advances of Government funds shall be withdrawn pursuant to a letter of credit in favor of the Contractor or the Contractor's bank, or, in the option of the Government, shall be made by check payable to the Contractor and shall be deposited only in the Special Bank Account established by an Agreement for Special Bank Account in the form and containing the provisions set forth in Appendix C of this contract. The Contractor shall likewise deposit in the Special Bank Account any other revenues received by the Contractor in connection with the work under this contract. No part of the funds in the Special Bank Account shall be (a) mingled with any funds of the Contractor or (b) used for a purpose other than that of making payments for costs allowable under this contract or payments for other items specifically approved in writing by the Contracting Officer and payments of the Contractor's fixed fee as provided for elsewhere in this contract. If the Contracting Officer shall at any time determine that the balance on such bank account exceeds the Contractor's current needs, the Contractor shall promptly make such disposition of the excess as the Contracting Officer may direct.

4. *Title to Funds Advanced.* Title to the unexpended balance of any funds advanced and of any bank account established pursuant to this article shall remain in the Government and be superior to any claim or lien of the bank of deposit or others. It is understood that an advance to the Contractor hereunder is not a loan to the Contractor, and will not require

the payment of interest by the Contractor, and that the Contractor acquires no right, title, or interest in or to such advance other than the right to make expenditures therefrom as provided in this article.

5. *Review and Approval of Costs Incurred.* The Contractor shall prepare and submit annually as of June 30, a voucher, for the total of net expenditures accrued (i.e., net costs incurred) for the period covered by the voucher, and the Commission, after audit and appropriate adjustment will approve such voucher. This approval by the Commission will constitute an acknowledgment by the Commission that the net costs incurred are allowable under the contract and that they have been recorded in the accounts maintained by the Contractor in accordance with the Commission accounting policies, but will not relieve the Contractor of responsibility for the Commission's assets in its care, for appropriate subsequent adjustments, or for errors later becoming known to the Commission.

* * * * *

9. *Revenues.* All revenues other than the Contractor's fixed fee or fees, if any, accruing to the Contractor in connection with the work under this contract shall be Government property and shall be deposited in the Special Bank Account to be available for payment of allowable cost under this contract.

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ARTICLE IX—CONTRACTOR PROCUREMENT

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4. In addition to procurement for its activities under this contract and for Constructors for the work under Contract No. AT(29-1)-1357, the Contractor shall procure such items for the use of the Commission and other Commission contractors as may be required by the Contracting Officer from time to time to the extent that funds are made available therefor by the Commission. This procurement for others shall be performed by the same methods, practices, and proce-

dures found acceptable by the Contracting Officer for the Contractor's own activities.

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ARTICLE XII—PROPERTY

1. *Furnishing of Government Property.* The Government reserves the right to furnish any property or services required for the performance of the work under this contract.

2. *Title to Property.* Title to all property furnished by the Government shall remain in the Government except as otherwise provided in this article. Except as otherwise provided by the Contracting Officer, title to all materials, equipment, supplies, and tangible personal property of every kind and description purchased by the Contractor, for the cost of which the Contractor is entitled to be reimbursed as a direct item of cost under this contract, shall pass directly from the vendor to the Government. The Government reserves the right to inspect, and to accept or reject, any item of such property. The Contractor shall make such disposition of rejected items as the Contracting Officer shall direct. Title to other property, the cost of which is reimbursable to the Contractor under this contract, shall pass to and vest in the Government upon (i) issuance for use of such property in the performance of this contract, or (ii) commencement of processing or use of such property in the performance of this contract, or (iii) reimbursement of the cost thereof by the Government, whichever first occurs. Property furnished by the Government and property purchased or furnished by the Contractor, title to which vests in the Government under this section, are hereinafter referred to as Government property. Title to Government property shall not be affected by the incorporation of the property into or the attachment of it to any property not owned by the Government, nor shall such Government property, or any part thereof, be or become a fixture or lose

its indentity as personalty by reason of affixation to any realty.

* * * * *

9. *Property Management.* The Contractor shall establish and maintain a property management system, acceptable to the Contracting Officer, including stock control and disposal providing for all phases of supply activities and designed to procure, utilize, protect and control all property adequately. The property management system that has been approved by the Contracting Officer and is now in effect shall not be changed without the approval of the Contracting Officer. The property management activities shall be subject to inspection and audit by the Commission at all reasonable times.

* * * * *

EXCERPTS FROM ATOMIC ENERGY COMMISSION CONTRACT AT(29-1)-1357 DATED JULY 1, 1970, WITH LOS ALAMOS CONTRACTORS, INC. (R. II)

* * * * *

ARTICLE III—TERM

The term of this contract shall extend through June 30, 1975, unless sooner terminated in accordance with the provisions of the article entitled "Termination." At least six months prior to said June 30, 1975, the parties will confer to determine whether the contract should be extended, and if so, upon what terms. If the parties are unable to agree upon a basis for extending the contract term beyond the above date, the Commission may require the Contractor to perform for an additional period of six months or less beyond June 30, 1975, all or any part of the work which the Contractor is then performing under this contract, at a fee to be agreed upon by the parties as proportionate to the fee covering the final full fiscal year of this contract, based upon the estimated amount and character of the work to be performed during such additional period, as compared with the amount and character of work performed by the Contractor during such final full fiscal year. A failure to agree on such a fee under this article shall be deemed to be a dispute within the meaning of the article entitled "Disputes". Nothing contained in this article shall excuse the Contractor from proceeding with the prosecution of the work in accordance with the requirements of the Commission hereunder.

ARTICLE IV—PROGRAM DEVELOPMENT AND FINANCIAL PLANS; OBLIGATION OF FUNDS

1. *Program Development and Financial Plans.* Work programs and estimates of cost shall be developed on the basis of each fiscal year during the term of this contract. * * *

* * * * *

2. *Obligation of Funds.* The amount presently obligated by the Government with respect to this contract is Sixteen Million Eight Hundred Nine Thousand Dollars ($16,809,000.00). Such amount may be increased unilaterally by the Commission by written notice to the Contractor and may be increased or decreased by written agreement of the parties (whether or not by formal modification of this contract). Estimated revenues and receipts from others from work and services to be performed under this contract are not included in the amount obligated with respect to this contract. Such revenues and receipts, to the extent actually received by the Contractor, shall be available and used for the payment of allowable costs as provided in the article entitled "Payments and Advances." Nothing in this Paragraph 2. is to be construed as authorizing the Contractor to exceed limitations stated in financial plans established by the Commission and furnished to the Contractor from time to time under this contract.

3. *Limitation on Payment by the Government.* Except as otherwise provided in this contract and except for costs which may be incurred by the Contractor pursuant to the article entitled "Termination" or costs of claims allowable under the contract accruing after completion or termination and not released by the Contractor at the time of financial settlement of the contract in accordance with the article entitled "Payments and Advances", payment by the Government under this contract on account of allowable costs shall not in the aggregate exceed the amount obligated with respect to this contract, less the Contractor's fixed fee. Unless expressly negated in this contract, payment on account of those costs excepted in the preceding sentence which are in excess of the amount obligated with respect to this contract shall be subject to the availability of (a) revenues and receipts deposited to the Government's account as provided in the article entitled "Payments and Ad-

vances", and (b) other funds which the Commission may legally use for such purpose; provided, the Commission will use its best efforts to obtain the appropriation of funds for this purpose if not otherwise available.

4. *Notices—Contractor Excused from Further Performance.* The Contractor shall notify the Commission in writing whenever the unexpended balance of funds (including revenues and receipts) available under Paragraph 2. above, plus the Contractor's best estimate of revenues and receipts to be received during the ninety day period hereinafter specified, is in the Contractor's best judgment sufficient to continue contract operations at the programmed rate for only ninety days and to cover the Contractor's unpaid fixed fee, and outstanding commitments and liabilities on account of costs allowable under the contract at the end of such period. Whenever the unexpended balance of funds (including revenues and receipts) available under Paragraph 2. above, less the amount of the Contractor's fixed fee then earned but not paid, is in the Contractor's best judgment either sufficient only to liquidate outstanding commitments and liabilities on account of costs allowable under this contract or is equal to zero, the Contractor shall immediately notify the Commission and shall make no further commitments or expenditures (except to liquidate existing commitments and liabilities), and, unless the parties otherwise agree, the Contractor shall be excused from further performance (except such performance as may become necessary in connection with termination by the Government) and the performance of all work hereunder will be deemed to have been terminated for the convenience of the Government in accordance with the provisions of the articles entitled "Termination".

5. *Financial Plans; Cost and Commitment Limitations.* In addition to the limitations provided for elsewhere

in this contract, the Commission may, through financial plans or other directives issued to the Contractor, establish controls on the cost to be incurred and commitments to be made in the performance of the contract work. Such plans and instructions may be amended or supplemented from time to time by the Commission. The Contractor hereby agrees to comply with the specific limitations (ceilings) on costs and commitments set forth in such plans and directives, to use its best efforts to comply with the other requirements of such plans and directives, and to promptly notify the Commission in writing whenever it has reason to believe the authorized financial levels of costs and commitments will be exceeded or substantially underrun.

6. *Government's Right to Terminate not Affected.* The giving of any notice under this article shall not be construed to waive or impair any right of the Government to terminate the contract under the provisions of the article entitled "Termination".

ARTICLE V—CHANGES

1. *Changes and Adjustment of Fee.* The Contracting Officer may at any time and without notice to the sureties, if any, issue written directions within the general scope of this contract requiring additional work or directing the omission of or variation in work covered by this contract. If any such direction results in a material change in the amount or character of the work described in the article entitled "Statement of Work", an equitable adjustment of the fixed-fee shall be made in accordance with the agreement of the parties and the contract shall be modified in writing accordingly. • • •

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ARTICLE VII—PAYMENTS AND ADVANCES

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3. *Special Bank Account—Use.* All advances of Government funds shall be withdrawn pursuant to a letter of credit in favor of the Contractor or the Contractor's bank or, in the option of the Government, shall be made by check payable to the Contractor and shall be deposited only in the Special Bank Account established by an Agreement for Special Bank Account in the form and containing the provisions set forth in Appendix C of this contract. The Contractor shall likewise deposit in the Special Bank Account any other revenues received by the Contractor in connection with the work under this contract. No part of the funds in the Special Bank Account shall be (a) mingled with any funds of the Contractor or (b) used for a purpose other than that of making payments for costs allowable under the contract or payments for other items specifically approved in writing by the Contracting Officer and payments of the Contractor's fixed fee as provided for elsewhere in this contract. If the Contracting Officer shall at any time determine that the balance on such bank account exceeds the Contractor's current needs, the Contractor shall promptly make such disposition of the excess as the Contracting Officer may direct.

4. *Title to Funds Advanced.* Title to the unexpended balance of any funds advanced and of any bank account established pursuant to this article shall remain in the Government and be superior to any claim or lien of the bank of deposit or others. It is understood that an advance to the Contractor hereunder is not a loan to the Contractor, and will not require the payment of interest by the Contractor, and that the Contractor acquires no right, title, or interest in or to such advance other than the right to make expenditures therefrom as provided in this article.

5. *Review and Approval of Costs Incurred.* The Contractor shall prepare and submit annually as of June 30, a voucher, for the total of net expenditures accrued (i.e., net costs incurred) for the period covered by the voucher, and the Commission, after audit and appropriate adjustment will approve such voucher. This approval by the Commission will constitute an acknowledgement by the Commission that the net costs incurred are allowable under the contract and that they have been recorded in the accounts maintained by the Contractor in accordance with the Commission accounting policies, but will not relieve the Contractor of responsibility for the Commission's assets in its care, for appropriate subsequent adjustments, or for errors later becoming known to the Commission.

6. *Financial Settlement.* The Government shall promptly pay to the Contractor the unpaid balance of allowable costs and fixed fee upon termination of the work, expiration of the term of the contract, or completion of the work and its acceptance by the Government after (1) compliance by the Contractor with the Commission's patent clearance requirements, and (2) the furnishing by the Contractor of:

a. An assignment of the Contractor's rights to any refunds, rebates, allowances, accounts receivable, or other credits applicable to allowable costs under the contract;

* * * * *

9. *Revenues.* All revenues other than the Contractor's fixed fee or fees, if any, accruing to the Contractor in connection with the work under this contract shall be Government property and shall be deposited in the Special Bank Account to be available for payment of allowable cost under this contract.

* * * * *

ARTICLE IX—CONTRACTOR PROCUREMENT

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2. In addition to, and without derogation of any rights under section 1. of this article and any other provision in this contract, the Contractor shall require subcategories to furnish cost or pricing data, and shall include in such subcontracts the clause set forth in AECPR 9-3.814-50, except as otherwise directed or approved by the Commission.

3. Procurement or transfer of equipment, materials, supplies, or services from a Contractor-controlled source [any division or other organizational component of the prime contractor (exclusive of the contracting component) and any subsidiary or affiliate of the Contractor under a common control] shall be considered a procurement for the purposes of this article, excepting procurement or transfers from Constructors under Contract No. AT (29-1)-1357.

4. In addition to procurement for its activities under this contract and for Constructors for the work under Contract No. AT(29-1)-1357, the Contractor shall procure such items for the use of the Commission and other Commission contractors as may be required by the Contracting Officer from time to time to the extent that funds are made available therefor by the Commission. This procurement for others shall be performed by the same methods, practices, and procedures found acceptable by the Contracting Officer for the Contractor's own activities.

ARTICLE X—ACCOUNTS, RECORDS, AND INSPECTION

1. *Accounts.* The Contractor shall maintain a separate and distinct set of accounts, records, documents and other evidence showing and supporting all allowable costs incurred, revenues or other applicable credits, fixed-fee accruals, and the receipt, use, and disposition of all Government property coming into the possession of the Contractor under this contract. The system of

accounts employed by the Contractor shall be satisfactory to the Commission and in accordance with generally accepted accounting principles consistently applied and shall not be changed without the prior approval of the Contracting Officer.

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ARTICLE XI—EXAMINATION OF RECORDS

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3. Nothing in this contract shall be deemed to preclude an audit by the General Accounting Office of any transaction under this contract.

ARTICLE XII—PROPERTY

1. *Furnishing of Government Property.* The Government reserves the right to furnish any property or services required for the performance of the work under this contract.

2. *Title to Property.* Title to all property furnished by the Government shall remain in the Government except as otherwise provided in this article. Except as otherwise provided by the Contracting Officer, title to all materials, equipment, supplies, and tangible personal property of every kind and description purchased by the Contractor, for the cost of which the Contractor is entitled to be reimbursed as a direct item of cost under this contract, shall pass directly from the vendor to the Government.

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EXCERPTS FROM ATOMIC ENERGY COMMISSION CONTRACT AT(29-1)-789, 12/31/73, W/WESTERN ELECTRIC CO. (R.II)

CONTRACT AT(29-1)-789

between

UNITED STATES ATOMIC ENERGY COMMISSION

and

WESTERN ELECTRIC COMPANY, INCORPORATED

Modification No. 29

Dated December 31, 1973

Effective January 1, 1974

Including as Appendix A
the Contract between
SANDIA CORPORATION

and

WESTERN ELECTRIC COMPANY, INCORPORATED

Dated December 31, 1973

Effective January 1, 1974

ARTICLE III. Reimbursement of Costs

1. The services of Sandia Corporation and of Western, Bell Laboratories, and any other Bell System company which may be called upon to render services hereunder, other than communication services, shall be rendered without fee or profit of any kind.

2. Since Sandia Corporation was created for the purpose of operating Commission facilities and performing work under this Contract and will engage in no activities other than as herein provided, all costs and expenses incurred by Sandia Corporation during the term hereof shall be reimbursed by the Commission, including, specifically, payments by Sandia Corporation to Western pursuant to the contract hereto attached as Appendix A and, in view of the fact that such undertaking was requested by the Government and contemplated that Western should sustain no loss thereby, it is agreed that no cost or expense shall be denied reimbursement as outside the scope of this Contract, unless the Commission shall establish that such cost or expense resulted from willful misconduct or bad faith on the part of some corporate officer or officers of Sandia Corporation or of any other person having complete or substantially complete charge of the Sandia Albuquerque or Livermore Laboratories. Any dispute as to whether such an item is reimbursable shall be determined pursuant to Article XII, Disputes.

3. Sandia Corporation may make advances to subcontractors, suppliers, and materialmen for labor or services or may pay for materials in advance of delivery, provided that the prior written approval of the Commission shall be obtained for any such advance in excess of $15,000.

4. Sandia Corporation shall apply all revenues received in its operations hereunder in reduction of costs here-

under, except as shall be otherwise directed in writing by the Commission.

5. Financial Plan, Costs Limitation. In addition to the limitations provided for elsewhere in this Contract, the Commission may through Financial Plans issued to Sandia Corporation establish controls on the costs to be incurred in the performance of the contract work. Such plans may be amended or supplemented from time to time by the Commission. Sandia Corporation agrees to use its best efforts to comply with such plans and to notify the Commission promptly in writing whenever it has reason to believe the authorized financial levels of costs will be exceeded or substantially underrun. Sandia Corporation hereby agrees to comply with specific limitations (ceilings) on costs as discussed with and accepted by Sandia Corporation in advance and as set forth in such plans.

ARTICLE IV. Advances and Vouchering

1. Neither Western nor Sandia Corporation shall be required to provide funds for operations under this Contract.
2. The Commission shall provide funds by either of the following methods or by any other method mutually agreed upon by Sandia Corporation and the Commission:
   a. by periodic advances to Sandia Corporation of the estimated amount required for the succeeding period disbursements, making supplementary advances whenever necessary, or
   b. by means of a Letter of Credit as authorized through the United States Treasury Department to a Federal Reserve Bank for the account and responsibility of the Commission and in favor of Sandia Corporation. Payment vouchers will be drawn by Sandia Corporation against the Letter

of Credit as needed for daily disbursements. All such advances or payment voucher proceeds and revenues received shall (except for petty cash and working balances) be deposited in special bank accounts under arrangements approved by the Commission.

3. Disbursements by Sandia Corporation hereunder shall apply against funds provided pursuant to Paragraph 2. of this Article IV in accordance with arrangements mutually agreed upon by Sandia Corporation and the Commission.

4. The total amount which Sandia Corporation is authorized to expend or commit under this Contract and which shall be a charge against such obligational authority as the Commission shall designate, shall be the then current total obligation of this Contract established by the Commission from time to time and evidenced by a certificate of the Manager, Albuquerque Operations Office, less the amounts previously committed by Sandia Corporation. The total obligation of this Contract will be increased by the Commission from time to time, in accordance with agreed quarterly estimates, to authorize commitments on approved programs of work and to provide for payment of costs incurred under this Contract. In addition to said total, Sandia Corporation is authorized to expend or commit under this Contract such additional sums as may be specified in "cash purchase orders" received by Sandia Corporation from other Commission Contractors and other revenues received.

ARTICLE V. Assumption of Risk by Government

1. The parties recognize that the work under this Contract involves unusual, unpredictable and abnormal risks. In view of these circumstances and the no-profit feature of this Contract, neither Western, San-

dia Corporation, Bell Laboratories, nor any company of the Bell System, shall be liable for, and the Government shall indemnify and hold them harmless against, any delay, failure, loss, expense (including expense of litigation), or damage (including personal injuries and deaths of persons and damage to property) of any kind and for any cause whatsoever, arising out of or connected with the work, and whether or not any employee or employees of any such company is or are responsible therefor. Provided, that neither Western, Sandia Corporation, Bell Laboratories, nor any company of the Bell System, shall be indemnified and held harmless for any cost or expense denied reimbursement pursuant to Article III, Paragraph 2. * * *

* * * * *

ARTICLE VI. Property

1. Title to all property of any kind whatsoever acquired by Sandia Corporation shall pass to the Government when it passes from the vendor, except as may be directed by the Commission. Sandia Corporation may transfer or otherwise dispose of Government-owned property in its possession to such parties and upon such terms and conditions as the Commission may approve.

* * * * *

ARTICLE IX. Patents and Inventions

1. Whenever any invention or discovery is made or conceived (a) by an employee of Sandia Corporation (other than such clerical or manual labor personnel as will not have access to technical data) in the course of, in connection with, or under the terms of this Contract or (b) by any employee of a Bell System company during the period of his loan to Sandia Corporation, pursuant to Item 2. of Article II of Appendix A, or in the performance of work pursuant to Item 3. or

7. of said Article, Sandia Corporation shall furnish the Commission with complete information thereon; and the Commission shall have the sole power to determine whether or not and where a patent application shall be filed, and to determine the disposition of the title to and the rights under any application or patent that may result and the judgment of the Commission on these matters shall be final; provided, however, that in any event there shall be reserved to Western, American Telephone and Telegraph Company and other companies of the Bell System nonexclusive, irrevocable, royalty-free licenses under said patents limited to make and to have made, use, lease and sell public service communication equipment. Except as otherwise authorized in writing by the Commission, Sandia Corporation will obtain from all such employees patent agreements and other documents to effectuate the purpose of this paragraph.

2. Under all patents now or during the term of this Contract owned or controlled by Western or as to which it has the right to grant licenses, without incurring an obligation to pay royalties or other compensation solely on account of the licenses herein granted, the invention or inventions of which are embodied or utilized by Sandia Corporation during the term of this Contract in the manufacture, design or development of Sandia Corporation products that utilize fissionable material or atomic energy for a military weapon or are otherwise used in or with such atomic energy military weapon, Western hereby grants and agrees to grant to the Government an irrevocable, nonexclusive, royalty-free license for the entire terms of said patents, to make and to have made, to use and to have used and to dispose of said products according to law.

* * * * *

ARTICLE XI. General. . . .

2. Procurement shall be conducted by Sandia Corporation in accordance with the policies and practices as agreed upon by Sandia Corporation and the Commission. The starting point shall be the policies and practices of Sandia Corporation in effect on the 1st day of January, 1974. If either Sandia or the Commission desires to propose changes in Sandia's procurement policies and practices, such proposed changes shall be submitted in writing to the other party and such changes, unless objected to as hereinafter provided, shall become effective 30 days after receipt of the proposed change. If either Sandia or the Commission desires to object to the proposed change they shall object in writing, prior to the expiration of said 30-day period, setting forth in detail their grounds of objection. If such an objection is made the parties shall meet to resolve the questions and, pending such resolution, the Sandia policies and practices in effect prior to the proposed change shall remain in force.

Sandia Corporation shall, in accordance with such policies and practices, be responsible for determining the kind and quantity of materials to be procured, selection of and negotiations with suppliers, negotiation of price or price basis and other purchase terms and conditions and audit and settlement of vendors' accounts; provided, however, that any procurement transaction in excess of $100,000 shall be subject to written approval of the Commission, and in such cases Sandia Corporation shall also furnish to the Commission a copy of its written justification, indicating the considerations on which the procurement is considered to be most advantageous to the Government, taking into consideration price, quality and other factors. All purchase orders, subcontracts and other commit-

ments shall be made in the name of Sandia Corporation, and shall (excepting contracts of employment) be reduced to writing if for more than $250. Sandia Corporation shall insert in such purchase orders, subcontracts and other commitments, such clauses as are required by statute, and Executive Order, and such clauses respecting Government property, security, patent rights, taxes, retention of records, Contract Work Hours and Safety Standards Act—Overtime Compensation, Davis-Bacon Act, Equal Opportunity, Walsh-Healey Public Contracts Act, Buy American Act, Renegotiation Act, Service Contract Act of 1965 and contingent fees, as the Commission may require. Sandia Corporation shall insert into its purchase orders, subcontracts and other commitments, let on a cost reimbursement basis and on a fixed price basis when the costs incurred are a factor in future price redeterminations, examination of records provisions as the Commission may require. Sandia Corporation shall observe the Commission's requirements respecting acquisition and use of property, supplies and transportation services available to the Government.

3. Sandia Corporation shall use a system of accounting and property control conforming to sound accounting principles, followed by Western and adapted to provide accounting and property information required by the Commission.

4. Sandia Corporation shall conform to all health, safety and fire protection regulations and requirements of the Commission, and shall take all reasonable steps and precautions to protect health and minimize danger from all hazards to life and property.

5. Western shall be responsible for, and shall supervise, performance by Sandia Corporation of its obligations under Paragraphs 1. through 3. of this Article. At least once annually Western shall audit the records

and review the practices of Sandia Corporation under Paragraphs 1. through 3. of this Article and shall furnish to the Commission copies of such audit report.

6. If the General Manager of the Commission shall raise a question with Western as to the reasonableness of any practice followed pursuant to Paragraphs 1. through 5. of this Article, which shall not be settled by mutual agreement, then the question shall be determined by the Commission itself and its determination shall be binding on Western, Sandia Corporation and the Government.

7. Sandia Corporation shall report to the Commission on activities under this Contract in such form and at such time as may be required by the Commission. The Commission shall have the right at all reasonable times to inspect and audit in such manner as it deems appropriate all activities of Sandia Corporation.

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APPENDIX A

This Contract made the 31st day of December, 1973, by and between SANDIA CORPORATION (hereinafter referred to as "Sandia"), a corporation of the State of Delaware, and WESTERN ELECTRIC COMPANY, INCORPORATED (hereinafter referred to as "Western"), a corporation of the State of New York;

WITNESSETH THAT:

WHEREAS, Western has entered into Modification No. 29 of Contract No. AT(29-1)-789 with the United States of America, acting through the Atomic Energy Commission (hereinafter referred to as the "Commission"), to continue to furnish the services provided for therein; and . . .

NOW THEREFORE, in consideration of the premises and of the mutual covenants herein contained, the parties hereto agree that the contract between the parties as heretofore amended, shall, effective as to performance starting January 1, 1974, be amended to read in its entirety as follows: . . .

ARTICLE II. Scope of the Work

Western shall:

Item 1. Transfer of Employees. From time to time select such of the management and technical personnel of the Bell System as Western may deem to be needed on a full-time basis for the work under Contract AT(29-1)-789. . .

Item 3. Laboratories Research and Development. Arrange for Bell Telephone Laboratories, Incorporated (herein referred to as the "Laboratories") to do such research and development in connection with the work under Contract AT(29-1)-789 as the Commission shall approve and Western and Sandia may deem the Labora-

tories is peculiarly fitted for and in a position to undertake;

Item 4. Products of Western. Furnish products of Western on terms and conditions agreed upon from time to time, provided that the prior written approval of the Commission shall be obtained for any purchase exceeding $500;

Item 5. Supervision and Audit. Furnish services and incur costs and expenses as required for performance by Western of its obligations under Article XI of said Modification No. 29 of Contract AT(29-1)-789;

Item 6. Headquarters Staff. Furnish services of executives of Western and the Laboratories and of Western's headquarters staff to the extent that Western and Sandia may deem them needed, ...

Item 7. General. Furnish such additional services and incur such additional costs and expenses incidental to or necessary for the performance and experimentation or termination of Contract AT(29-1)-789 as shall from time to time be agreed upon by Western and Sandia.

ARTICLE III. Reimbursement of Costs and Payment

Sandia shall reimburse Western and shall pay to Western, upon submission of invoices therefor monthly or as otherwise agreed by the parties, the following:

1. *Transferred Employees.* With respect to employees transferred to the employ of Sandia under Item 1. of Article II, (a) sums payable monthly, determined by applying to the aggregate salaries paid by Sandia to employees so transferred by each employer granting leaves of absence for such employment, the current pension and group insurance accrual rates, as adjusted from time to time, used by it in making payments into its Pension Trust Fund or for group insurance, as the case may be; and (b) sums equal to disability and death benefits paid to such employees, or their beneficiaries, pursuant to Article IV, plus an amount derived by ap-

plying said current pension and group insurance accrual rates to such disability benefits.

2. *Loaned Employees and Auditing Services.* With respect to employees loaned to Sandia under Item 2. of Article II and employees performing auditing services furnished under Item 5. of Article II, sums equal to the salaries paid to said employees by their employers during the period of such performance, plus (a) amounts derived by application to such sums of a rate to be negotiated following the close of each rate period to cover the employer's other employment costs (including employee security accruals, vacation, holiday, sickness and absence allowances and other payroll taxes and payroll expense) and (b) travel and living expense while away from their work location computed in accordance with their employer's normal practice. The rates referred to in (a), above, shall be negotiated on the basis of actual cost experience for the period, shall be reviewed by the Commission (which review may include such audit as the Commission may require), and the new rate agreed to be in effect for each period shall be incorporated in a supplement to this Contract. The rate period shall be the calendar year. Pending the establishment of a negotiated rate for any period, provisional payment shall be made at a billing rate approved by the Commission.

3. *Laboratories Research and Development.* For research and development by the Laboratories under Item 3. of Article II, reimbursement for expenditures incidental to and necessary for the performance of such work, in accordance with the provisions of Schedule A hereto attached.

4. *Products of Western.* For products of Western furnished under Item 4. of Article II, agreed prices, which in the case of standard products shall be those applicable from time to time to Western's sales of such products to the Government and which in the case of other products shall be approved by the Commission.

5. *Other Services and Costs.* For services furnished and in reimbursement of Western's and the Laboratories' costs and expenses furnished or incurred such sums as may be agreed upon by Western and Sandia, subject to approval by the Commission, as follows:

(a) With respect to supervisory services under Item 5., "Supervision and Audit," and with respect to Item 6., "Headquarters Staff," based upon a statement to be submitted by Western prior to the beginning of each quarter, covering services to be furnished during such period.

(b) With respect to Item 7., "General," based upon statements to be submitted by Western from time to time as such services are agreed upon or such costs and expenses are incurred.

6. *Refunds.* Rebates, discounts, refunds and any other similar revenues obtained by Western in connection with this Contract shall be applied in reduction of Western's costs hereunder.

ARTICLE IV. Status of Transferred Employees

Employees transferred under Item 1. of Article II, on leaves of absence from their prior employers, shall be employees of Sandia and under its sole control. The initial salary to be paid by Sandia to such employees and subsequent increases in salary shall be as agreed by Sandia and Western, having in view the eventual return of such employees to their prior employment. Such employees who become disabled or die while in the employ of Sandia, or their beneficiaries, shall receive from the employer granting leave of absence for such employment, accident and sickness and disability benefits and death benefits equal to those that, in accordance with the "Plan for Employees' Pensions, Disability Benefits and Death Benefits" of said employer, would have been payable if they had remained in such prior employment.

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SCHEDULE A

(attached to Contract between Sandia Corporation and Western Electric Company, Incorporated, as amended December —, 1973, effective January 1, 1974)

Reimbursement for expenses incidental to and necessary for performance of research and development by the Laboratories under Item 3. of Article II, as provided in Paragraph 3. of Article III of the attached contract, shall consist of the following:

(a) The cost to the Laboratories of materials charged in accordance with sound accounting methods consistently followed by the Laboratories, pursuant to which due credit is recognized in overhead for any scrap or surplus materials which are sold, including (i) the net cost to the Laboratories, after deducting all discounts, of materials and parts purchased directly for the performance of this Contract; (ii) the cost to the Laboratories of articles customarily produced or assembled by Western in the regular course of its business; (iii) the cost to the Laboratories of materials, not covered by the preceding section (ii), withdrawn from store or stockrooms other than the Laboratories'.

(b) The salaries and wages of scientists, technicians, draftsmen, workmen and others directly engaged in the performance of work hereunder and properly allocable thereto as recorded by departments in the Laboratories' accounts, and at rates computed in accordance with sound accounting methods consistently followed by the Laboratories.

(c) Cost of transportation and subsistence customarily allowed by the Laboratories for all personnel while in travel status, communication expenses, and incoming and outgoing shipping charges incurred directly in the performance of this Contract.

(d) Purchase, construction and installation or rental cost to the Laboratories of facilities necessary for the performance of this Contract, including machinery, furniture and fixtures, tools, test equipment and similar items.

(e) Cost to the Laboratories of services performed in accordance with the provisions of this Contract and supplied by other concerns including the cost to the Laboratories of services performed for the Laboratories by other Bell System companies and the cost to the Laboratories of services supplied by employees of Western and others), not otherwise provided for herein.

(f) The cost of correction and/or replacement of rejected material and/or workmanship and the cost of any rectifications required in connection with the work called for under this Contract, whether before or after completion of such work as well as the cost of any restoration or repairs of such work occasioned by or in connection with inspection, demonstration, use or test thereof.

(g) Such other costs to the Laboratories as shall by agreement of the parties hereto, and with the approval of the Commission, be included in the cost of the work.

(h) Costs of the above character incurred prior to but in anticipation of the execution of this Contract.

(i) Overhead, indirect charges and other elements of costs of the Laboratories not specifically recovered in direct charges hereunder computed by the application of overhead rates (negotiated as described in subparagraph (k) below) to salaries and wages included in subparagraph (b) of employees in the respective departments of the Laboratories.

(j) A reasonable and proper proportionate share of Western's cost of administration applicable and allocable to the performance of Item 3. of Article II of this Contract, other than costs incurred by the Laboratories, and a reasonable and proper proportionate share of expense of general engineering performed by Western and the Laboratories in connection with Government business which, because of its nature and scope, cannot be related

specifically to individual orders and projects, computed by the application of overhead rates (negotiated as described in subparagraph (k), below) to the total of sums payable under subparagraphs (a) to (i), inclusive.

(k) The overhead rates to be applied under this Contract under subparagraphs (i) and (j), above, shall be those negotiated by Sandia and Western for successive calendar year periods and approved by the Commission on the basis of actual cost experience for each such period as determined by audit. Any such audit may be performed, at the option of the Commission, by a Department of Defense audit agency, by the Commission itself, or by both. The actual overhead rates approved by the Commission to be in effect for each such period shall be incorporated in a supplement to this Contract. Pending the approval of overhead rates by the Commission for any such period provisional payment shall be made at billing rates approved by the Commission.

APPENDIX B

(D) *Compliance with Labor Statutes*

1. *Contract Work Hours and Safety Standards Act—Compensation.* . . .

   a. *Overtime Requirements.* Neither Sandia Corporation nor any subcontractor . . . may require . . . work in excess of eight hours in any calendar day . . . unless . . . compensation at a rate not less than one and one-half time . . . basic rate of pay for all such hours worked in excess of eight hours . . .

   b. *Violation; Liability for Unpaid Wages; Liquidated Damages.* In the event of any violation of the provisions of Paragraph a., Sandia Corporation and any subcontractor responsible therefor shall be liable to any affected employee for his unpaid wages. . . .

* * * * *

(P) *Conduct of Employees*

1. *President of Sandia Corporation.* During the performance of this Contract, the work provided for under the contract shall be under the direction of the President of Sandia Corporation who shall be a person acceptable to the Commission.

ZIA CONTRACT MODIFICATION NO. 66,
SUPPLEMENTAL EXH. TO PLAINTIFF'S
MOTION FOR SUMMARY JUDGMENT,
7/6/76, pp. 1 and 12 (R.II)

UNITED STATES ENERGY RESEARCH
AND DEVELOPMENT ADMINISTRATION
P. O. BOX 5400
ALBUQUERQUE, NEW MEXICO 87115

Modification No. 66
Supplemental Agreement to
Contract No. W-17-028-ENG-90

SUPPLEMENTAL AGREEMENT

THIS SUPPLEMENTAL AGREEMENT, entered into effective this 1st day of April 1976, by and between the UNITED STATES OF AMERICA (hereinafter called "Government"), represented by the UNITED STATES ENERGY RESEARCH AND DEVELOPMENT ADMINISTRATION (hereinafter called the "ERDA"), and THE ZIA COMPANY (hereinafter called the "Contractor") a corporation organized and existing under the laws of the State of Delaware.

WITNESSETH THAT:

WHEREAS, the Contractor is now performing services for the Government under Contract No. W-17-028-ENG-90, which was initially executed on behalf of the Government by the War Department on April 1, 1946; twice amended and as amended transferred to the United States Atomic Energy Commission on January 1, 1947, by Executive Order 9816; and thereafter amended by Modifications 3 through 65, which among other things extended the term through March 31, 1976; and

WHEREAS, it is now desired by the ERDA to extend the term of the contract through December 31, 1980; and

ARTICLE VI—ALLOWABLE COSTS AND FIXED FEE

1. *Compensation for Contractor's Services—Limitation of Government's Financial Obligations.* As compensation for the performance of the work under this contract, the Contractor shall be paid a fixed fee as hereinafter provided. It is understood and agreed, however, that the fixed fee shall be allowed the Contractor only for those services which are performed by the Contractor under Section 1.a. of the article entitled "Statement of Work," and that no fee shall be allowed the Contractor by the Government for those services which are performed by the Contractor for Constructors under Section 1.b. of such article. Payment to the Contractor of the fixed fee and payment, as herein provided, of the allowable cost, as hereinafter defined, shall constitute full and complete satisfaction of the Government's financial obligations under this contract.

2. *Fixed Fee.* The fixed fee payable to the Contractor for the performance of the work under this contract for the period April 1, 1976 through September 30, 1976, is One Hundred Sixteen Thousand Eight Hundred Dollars ($116,800.00). In agreeing upon the fixed fee to be paid, the amount and character of the work which the parties contemplated would be performed by the Contractor during the period April 1, 1976 through September 30, 1976, is that work reflected in the work program developed pursuant to the provisions of Paragraph 1.a. of the article entitled "Program Development and Financial Plans; Obligation of Funds." The presently estimated cost of such work is Ten Million Two Hundred Forty-eight Thousand Dollars ($10,248,000.00) exclusive of the Contractor's fixed fee.

MODIFICATION NO. 30 7/22/77 TO WESTERN ELECTRIC CO. CONTRACT NO. AT(29-1)-789 (R.II)

SUPPLEMENTAL AGREEMENT

This SUPPLEMENTAL AGREEMENT effective July 1, 1977, between THE UNITED STATES OF AMERICA (hereinafter called the "Government"), represented by the undersigned Contracting Officer of the UNITED STATES ENERGY RESEARCH AND DEVELOPMENT ADMINISTRATION (hereinafter called "ERDA"), previously represented by the UNITED STATES ATOMIC ENERGY COMMISSION (hereinafter called the "Commission"), and WESTERN ELECTRIC COMPANY, INCORPORATED (hereinafter called "Western"), a corporation of the State of New York,

WITNESSETH THAT:

WHEREAS, effective July 1, 1949, the Commission and Western entered into this contract for the operation of facilities and performance of work as herein provided; and

WHEREAS, the contract has been amended by Modifications 1 through 29; and

WHEREAS, effective January 19, 1975, the Commission was abolished and ERDA was established pursuant to the Energy Reorganization Act of 1974 (Public Law 93-438); and

WHEREAS, the functions and responsibilities of the Commission with respect to this contract have been transferred by operation of law to ERDA; and

WHEREAS, the parties recognize that under this contract and the long-standing relationship and practice of

the parties hereunder Sandia Corporation acts and has acted as an agent for and on behalf of ERDA and the Commission for certain purposes; and

WHEREAS, for the benefit of persons who are not parties and not familiar with the contractual relationships and practices hereunder, the parties desire to have the contract reflect the long-standing agency status and authority of Sandia Corporation for certain purposes; and

WHEREAS, this Supplemental Agreement is authorized by Public Law 93-438 and other applicable law.

NOW THEREFORE, the parties hereto agree that said Contract AT(29-1)-789, as previously amended, is further amended as follows:

The following article is added to the contract as Article XX:

Article XX. Status and Authority of Sandia Corporation as an Agent of ERDA

Under the provisions of this contract, Sandia Corporation has performed and will continue to perform as a management contractor of ERDA. On the basis of certain provisions of this contract and the long-standing relationship and practice of the parties hereunder, it is recognized that Sandia Corporation acts as an agent for and on behalf of ERDA for certain purposes. Particular provisions and features of the contractual relationship which establish the agency status of Sandia Corporation and the extent of the status and authority thereby created include, but are not limited to, the following:

1. Only ERDA funds are to be used in the performance of this contract by Sandia Corporation, and no funds of Sandia Corporation or of Western are required. The funds of ERDA made available for performance of this contract pursuant to

the provisions hereof and pursuant to any special bank accounts established hereunder, including all revenues received by Sandia Corporation in the conduct of operations hereunder, are and shall remain the funds of ERDA until expended and shall not at any time become the funds of Sandia Corporation or Western. Sandia Corporation acts as agent for and on behalf of ERDA in disbursing ERDA funds, by the drawing of checks on special bank accounts or by any other method approved by ERDA, for the payment and satisfaction of all obligations properly incurred by Sandia on behalf of ERDA in accordance with the provisions of this contract.

2. No property of Western is required to be used in performance of this contract. Sandia Corporation has no assets other than $1000 paid-in capital necessary for incorporation which is held in U.S. Government bonds. Except as provided in this contract and in performance thereof, Sandia Corporation shall not purchase or otherwise acquire property of any kind. Sandia Corporation in the performance of this contract acts as the agent of ERDA in the purchase, lease, or other acquisition, and in the management, maintenance, protection, safeguarding, sale, and disposition of all property of any kind whatsoever, real or personal, used in the performance of this contract.

3. All of the rights, benefits, and advantages flowing to Sandia Corporation from all transactions, contracts and other arrangements of any kind entered into by Sandia Corporation in performance of this contract in accordance with its terms are acquired by Sandia Corporation for the sole benefit of ERDA and on behalf of ERDA. Subject to compliance with other provisions of this contract, Sandia Corporation is authorized to

pledge the credit of the United States in any and all such transactions, contracts, and other arrangements.

4. ERDA considers all obligations properly incurred in accordance with the provisions of this contract to be ERDA obligations from their inception. Sandia Corporation acts as agent of ERDA in making appropriate payments to all obligees and is responsible for taking any and all other actions as may be necessary for appropriate and timely discharge of all such ERDA obligations. The purpose of this article is to recognize and express existing relationships. This article shall not be construed to modify any other provisions of the contract nor shall it create rights or obligations not otherwise provided for in the contract.

IN WITNESS WHEREOF, the parties hereto have executed this Supplemental Agreement in several counterparts.

THE UNITED STATES OF AMERICA

By: U.S. ENERGY RESEARCH AND DEVELOPMENT ADMINISTRATION

Date: 22 Jul. 1977

By: /s/ Herman E. Roser
Manager
Albuquerque Operations Office
Contracting Officer

ATTEST:

WESTERN ELECTRIC COMPANY, INCORPORATED

/s/ [Illegible]
Assistant Secretary

By: /s/ James G. Herbert
Executive Vice President

[SEAL]

Sandia Corporation hereby becomes a party to the above Supplemental Agreement, assuming all of the obligations therein imposed upon it.

ATTEST:

/s/ [Illegible]
Secretary

SANDIA CORPORATION

By: /s/ Morgan Sparks
President

MODIFICATION NO. M069 7/21/77 TO
ZIA CONTRACT NO. EY-76-C-04-0090, FORMERLY
CONTRACT NO. W-17-028-Eng-90 (R.II)

UNITED STATES ENERGY RESEARCH AND
DEVELOPMENT ADMINISTRATION
P.O. BOX 5400
ALBUQUERQUE, NEW MEXICO 87115

SUPPLEMENTAL AGREEMENT

This SUPPLEMENTAL AGREEMENT entered into effective July 1, 1977, by and between THE UNITED STATES OF AMERICA (hereinafter called the "Government"), represented by the UNITED STATES ENERGY RESEARCH AND DEVELOPMENT ADMINISTRATION (hereinafter called "ERDA"), and THE ZIA COMPANY (hereinafter called the "Contractor"), a corporation organized and existing under the laws of the State of Delaware.

WITNESSETH THAT:

WHEREAS, the Contrator is now performing services for the Government under Contract No. W-17-028-ENG-90, which was initially executed on behalf of the Government by the War Department on April 1, 1946; twice amended and as amended transferred to the United States Atomic Energy Commission on January 1, 1947, by Executive Order 9816; and thereafter amended by Modifications 3 through 65; thereafter, as amended, transferred to ERDA, redesignated Contract EY-76-C-04-0090 and further amended by Modifications 66 through 68; and

WHEREAS, the parties recognize that under this contract and the long-standing relationship and practice of the parties hereunder the Contractor acts and has acted as an agent for and on behalf of ERDA and the Commission for certain purposes; and

WHEREAS, for the benefit of persons who are not parties and not familiar with the contractual relationships and practices hereunder, the parties desire to have the contract reflect the long-standing agency status and authority of the Contractor for certain purposes; and

WHEREAS, this Supplemental Agreement is authorized by and executed under Public Law 93-438 and other applicable law in the interest of the common defense and security.

NOW THEREFORE, the parties hereto agree that the contract, as previously amended, is further amended in the following particulars only:

The following article is added to the contract as Article LIII:

ARTICLE LIII—STATUS AND AUTHORITY OF THE CONTRACTOR AS AN AGENT OF ERDA

Under the provisions of this contract, the Contractor has performed and will continue to perform as a management contractor of ERDA. On the basis of certain provisions of this contract and the long-standing relationship and practice of the parties hereunder, it is recognized that the Contractor acts as an agent for and on behalf of ERDA for certain purposes. Particular provisions and features of the contractual relationship which establish the agency status of the Contractor and the extent of the status and authority thereby created include, but are not limited to, the following:

1. Only ERDA funds are to be used in the performance of this contract by the Contractor, and no funds of the Contractor are required. The funds of ERDA made available for performance of this contract pursuant to the provisions hereof and pursuant to any special bank accounts established hereunder, including all revenues received

by the Contractor in the conduct of operations hereunder (excluding the fees paid to the Contractor), are and shall remain the funds of ERDA until expended and shall not at any time become the funds of the Contractor. The Contractor acts as agent for and on behalf of ERDA in disbursing ERDA funds, by the drawing of checks on special bank accounts or by any other method approved by ERDA, for the payment and satisfaction of all obligations properly incurred by the Contractor on behalf of ERDA in accordance with the provisions of this contract.

2. No property of the Contractor is required to be used or shall be used in performance of this concontract. In the performance of this contract the Contractor acts as the agent of ERDA in the purchase, lease, or other acquisition, and in the management, maintenance, protection, safeguarding, sale, and disposition of all property of any kind whatsoever, real or personal, used in the performance of this contract.

3. All of the rights, benefits, and advantages flowing to the Contractor from all transactions, contracts and other arrangements of any kind entered into by the Contractor in performance of this contract in accordance with its terms are acquired by the Contractor for the sole benefit of ERDA and on behalf of ERDA. Subject to compliance with other provisions of this contract, the Contractor is authorized to pledge the credit of the United States in any and all such transactions, contracts, and other arrangements.

4. ERDA considers all obligations properly incurred in accordance with the provisions of this contract to be ERDA obligations from their inception. The Contractor acts as agent of ERDA in

making appropriate payments to all obligees and is responsible for taking any and all other actions as may be necessary for appropriate and timely discharge of all such ERDA obligations.

The purpose of this article is to recognize and express existing relationships. This article shall not be construed to modify any other provisions of the contract (including, but not limited to, the article entitled Allowable Costs, Base Fee and Award Fee) nor shall it create rights or obligations not otherwise provided for in the contract.

IN WITNESS WHEREOF, the parties hereto have executed this Supplemental Agreement in several counterparts.

UNITED STATES OF AMERICA

By: ENERGY RESEARCH AND DEVELOPMENT ADMINISTRATION

Date: Jul 21 1977 By: /s/ Herman E. Roser
HERMAN E. ROSER,
Manager
Albuquerque Operations Office
Contracting Officer

THE ZIA COMPANY

Date: 7/21/77 By: /s/ Illegible
[Illegible]

Title: President

MODIFICATION NO. M059, 7/21/77 TO LACI CONTRACT NO. EY-76-C-04-1357, FORMERLY CONTRACT NO. AT(29 1)—1357 (R.II)

UNITED STATES
ENERGY RESEARCH AND DEVELOPMENT ADMINISTRATION
P. O. BOX 5400
ALBUQUERQUE, NEW MEXICO 87115

SUPPLEMENTAL AGREEMENT

This SUPPLEMENTAL AGREEMENT entered into effective July 1, 1977, by and between THE UNITED STATES OF AMERICA (hereinafter called the "Government"), represented by the UNITED STATES ENERGY RESEARCH AND DEVELOPMENT ADMINISTRATION (hereinafter called "ERDA"), and LOS ALAMOS CONSTRUCTORS, INC. (hereinafter called the "Contractor"), a corporation organized and existing under the laws of the State of New Mexico.

WITNESSETH THAT:

WHEREAS, the Contractor is now performing services for the Government under this contract, originally designated Contract AT(29-1)-1357, which was initially executed on behalf of the Government by the Atomic Energy Commission on March 31, 1953; thereafter amended by Modifications 1 through 55; thereafter, as amended, transferred to ERDA, redesignated Contract E(29-1)-1357, and subsequently redesignated Contract EY-76-C-04-1357 and further amended by Modifications 56 through 58; and

WHEREAS, the parties recognize that under this contract and the longstanding relationship and practice of the parties hereunder the Contractor acts and has acted as an agent for and on behalf of ERDA and the Commission for certain purposes; and

WHEREAS, for the benefit of persons who are not parties and not familiar with the contractual relationships and practices hereunder, the parties desire to have the contract reflect the long-standing agency status and authority of the Contractor for certain purposes; and

WHEREAS, this Supplemental Agreement is authorized by and executed under Public Law 93-438 and other applicable law in the interest of the common defense and security.

NOW THEREFORE, the parties hereto agree that the contract, as previously amended, is further amended in the following particulars only:

The following article is added to the contract as Article XLIX:

ARTICLE XLIX—STATUS AND AUTHORITY OF THE CONTRACTOR AS AN AGENT OF ERDA

Under the provisions of this contract, the Contractor has performed and will continue to perform as a management contractor of ERDA. On the basis of certain provisions of this contract and the longstanding relationship and practice of the parties hereunder, it is recognized that the Contractor acts as an agent for and on behalf of ERDA for certain purposes. Particular provisions and features of the contractual relationship which establish the agency status of the Contractor and the extent of the status and authority thereby created include, but are not limited to, the following:

1. Only ERDA funds are to be used in the performance of this contract by the Contractor, and no funds of the Contractor are required. The funds of ERDA made available for performance of this contract pursuant to the provisions hereof and pursuant to any special bank accounts es-

tablished hereunder, including all revenues received by the Contractor in the conduct of operations hereunder (excluding the fees paid to the Contractor), are and shall remain the funds of ERDA until expended and shall not at any time become the funds of the Contractor. The Contractor acts as agent for and on behalf of ERDA in disbursing ERDA funds, by the drawing of checks on special bank accounts or by any other method approved by ERDA, for the payment and satisfaction of all obligations properly incurred by the Contractor on behalf of ERDA in accordance with the provisions of this contract.

2. No property of the Contractor is required to be used or shall be used in performance of this contract. In the performance of this contract the Contractor acts as the agent of ERDA in the purchase, lease, or other acquisition, and in the management, maintenance, protection, safeguarding, sale, and disposition of all property of any kind whatsoever, real or personal, used in the performance of this contract.

3. All of the rights, benefits, and advantages flowing to the Contractor from all transactions, contracts and other arrangements of any kind entered into by the Contractor in performance of this contract in accordance with its terms are acquired by the Contractor for the sole benefit of ERDA and on behalf of ERDA. Subject to compliance with other provisions of this contract, the Contractor is authorized to pledge the credit of the United States in any and all such transactions, contracts, and other arrangements.

4. ERDA considers all obligations properly incurred in accordance with the provisions of this contract to be ERDA obligations from their inception. The

Contractor acts as agent of ERDA in making appropriate payments to all obligees and is responsible for taking any and all other actions as may be necessary for appropriate and timely discharge of all such ERDA obligations.

The purpose of this article is to recognize and express existing relationships. This article shall not be construed to modify any other provisions of the contract (including, but not limited to, the article entitled Allowable Costs, Base Fee and Award Fee and the provisions of the article entitled Statement of Work pertaining to the furnishing of certain services necessary for the work hereunder by Zia) nor shall it create rights or obligations not otherwise provided for in the contract.

IN WITNESS WHEREOF, the parties hereto have executed this Supplemental Agreement in several counterparts.

UNITED STATES OF AMERICA

By: ENERGY RESEARCH AND DEVELOPMENT ADMINISTRATION

Date: 7/21/77

By: /s/ Herman E. Roser
HERMAN E. ROSER
Manager
Albuquerque Operations Office
Contracting Officer

LOS ALAMOS CONSTRUCTORS, INC.

Date: Jul. 21, 1977

By: /s/ Illegible

Title: President

MEMO FROM JOHN McNETT
TO CHARLES ROSS, JR.
4/26/77, EXH. 11 to
DEFENDANTS' CROSS-MOTION
FOR SUMMARY JUDGMENT
(R.III)

April 26, 1977

Note to C. T. Ross, Jr., General Attorney,
Sandia Corporation

Charlie:

As I indicated in our recent discussion, the addition of "agency" language to the contract must be rather carefully considered in order that we not prejudice our case in prior years when such language did not appear in the contract. The language must also be drafted with both the gross receipts issue in mind, as well as the purchases issue.

With these thoughts in mind we have drafted a proposed additional article for the Western contract for your consideration and as a basis for further discussion. The draft is enclosed.

Let me know when you are ready to get together for some further discussion on both approaches.

9/6/77

The date of this note was incorrectly stated as 4/24/77 in my letter to Dan Friedman of 8/26/77. As a result the same error was made in item 8 of defendants' motion to compel discovery.

/s/ John F. McNett

Enclosure:

Draft article

EXHIBIT 13

LETTER FROM JOHN McNETT
TO DANIEL H. FRIEDMAN,
8/26/77, EXH. 13 TO
DEFENDANTS' CROSS-MOTION
FOR SUMMARY JUDGMENT
(R.III)

UNITED STATES ENERGY RESEARCH
AND DEVELOPMENT ADMINISTRATION
Albuquerque Operations Office
P.O. Box 5400
Albuquerque, New Mexico 87115

Aug. 26, 1977

Mr. Daniel H. Friedman
Attorney, Legal Division
Bureau of Revenue
State of New Mexico
Santa Fe, New Mexico 87503

UNITED STATES V. *STATE OF NEW MEXICO ET AL.*—CIVIL ACTION NO. 75-418M

Dear Dan:

This will confirm our discussions of August 23 and 24 concerning the answers to interrogatories served on defendants on August 22, 1977.

Since our answers were prepared, we have located an additional earlier draft of the modification to the Western contract. To account for this draft and a related note from ERDA to Sandia counsel, the chronological narrative should be revised by inserting the following sentence after the first sentence of the first full paragraph on page 7:

> "A subsequent revision of the initial rough draft was sent to Mr. Charles T. Ross by informal note from Leonard A. Jacobvitz dated April 24, 1977,

suggesting discussion of the draft by ERDA and Sandia counsel."

In addition, the last sentence of the first full paragraph on page 7 should be revised by inserting at the beginning the words: "Except for the draft attached to the Jacobvitz/Ross note of April 24, ..."

You indicated some concern with our answer to interrogatory 132. Our answer is intended to convey the idea that we gave no consideration to "designating" the contractors agents, as opposed to "recognizing" their existing agent status. To remove any doubt in this regard, please consider our answer amended by the addition of the following sentence at the end:

> 'No consideration was given by anyone at any time to 'formally and directly designating the contractors as agents for various purposes in the contract modifications.' "

You raised a question not specifically covered by your interrogatories concerning the statement in paragraph 3 of each of the modifications that the contractor "is authorized to pledge the credit of the United States" in all transactions. The use of the word "is" was not intended to imply that these are words of present authorization. This authority is no different from any other authority and status mentioned in the modifications—i.e., it is authority which the contractors have had all along and continue to have.

Sincerely,

/s/ John F. McNett
JOHN F. MCNETT
Assistant Chief Counsel

OGC:JFM

cc: Mr. John J. McCarthy, Chief
Civil Trial Section, Central Division
Tax Division
Room 3101, Old Star Building
U.S. Department of Justice
Washington, D.C. 20530

EXHIBIT 12

JOHN McNETT AFFIDAVIT,
9/9/77, EXH. 12 TO
DEFENDANTS' CROSS-MOTION
FOR SUMMARY JUDGMENT
(R.III)

IN THE UNITED STATES DISTRICT COURT FOR
THE DISTRICT OF NEW MEXICO

Civil Action No. 75-418M

UNITED STATES OF AMERICA, PLAINTIFF

vs.

STATE OF NEW MEXICO; BUREAU OF REVENUE OF THE STATE OF NEW MEXICO; and FRED L. O'CHESKEY, as Commissioner of Revenue of and for the State of New Mexico, and his successors in office, DEFENDANTS

MEMORANDUM OF DISCUSSIONS
FOR IN-CAMERA INSPECTION

The full identification of the persons referred to in this memorandum are, in alphabetical order, as follows:

1. Anthony G. Garretta, Assistant Director for Procurement Policy, Division of Procurement, ERDA Headquarters
2. John X. Combo, Chief Counsel, Idaho Operations Office, ERDA
3. Guy H. Cunningham, III, Assistant General Counsel for Litigation, ERDA Headquarters
4. Robert L. Forst, Deputy Assistant General Counsel for Procurement, ERDA Headquarters
5. Sally M. Gerety, Counsel, Los Alamos Area Office, ERDA
6. Richard L. Hames, Chief Counsel, Richland Operations Office, ERDA

7. Charles W. Hill, Chief Counsel, Oak Ridge Operations Office, ERDA

8. W. J. Howard, Executive Vice President, Sandia Corporation

9. Leonard A. Jacobvitz, Chief Counsel, Albuquerque Operations Office, ERDA

10. Hugh D. Leenhouts, Assistant Manager for Logistics, Albuquerque Operations Office, ERDA

11. John J. McCarthy, Chief, Civil Trial Section, Central Division, Tax Division, U.S. Department of Justice

12. John F. McNett, Assistant Chief Counsel, Albuquerque Operations Office, ERDA

13. Herman E. Roser, Manager, Albuquerque Operations Office, ERDA

14. Charles T. Ross, Jr., General Attorney, Sandia Corporation

15. Q. B. San Hamel, Attorney, Sandia Corporation

16. Dr. Morgan Sparks, President, Sandia Corporation

17. Charles E. Stratton, Trial Attorney, Civil Trial Section, Central Division, Tax Division, U.S. Department of Justice

18. W. L. Williamson, Attorney, Sandia Corporation

After I prepared my memorandum to Mr. Roser of March 2, 1977, I discussed it with Mr. Jacobvitz. I suggested that a copy be sent to Mr. Ross so that Sandia could be considering some of the matters discussed in my memorandum in connection with the renewal of the Western contract for the five-year period beginning October 1, 1978. The recommendations of the Albuquerque Operations Office for the five-year renewal of the Western contract were due in ERDA Headquarters in Washington 18 months in advance of the renewal date.

I pointed out to Mr. Jacobvitz that any agency language added to the contract would have to be carefully drafted to be consistent with the position we are taking in the litigation, both with respect to purchases by Sandia and the "gross receipts" or "advanced funding" issues.

Mr. Jacobvitz suggested that I prepare a draft article for Sandia's consideration.

Between the time of the above discussions and April 26, 1977, I worked intermittently on a contract article for the Western contract to express Sandia's "management contractor" role and to express existing agency relationships of Sandia to ERDA. I don't recall discussing my drafting efforts with anyone prior to April 26, 1977. In this drafting effort, I never considered any approach other than one of recognizing and expressing existing ERDA-Sandia roles and relationships. The result of this effort was a draft Article XX entitled "Relationship of the Parties," which was sent by Mr. Jacobvitz to Mr. Ross by informal note of April 26, 1977.

Sometime after April 26, 1977 (I don't recall the exact date), a meeting was held in Mr. Jacobvitz's office, attended by Mr. Ross, Mr. Williamson, Mr. Jacobvitz and me. The meeting was arranged by Mr. Ross and Mr. Jacobvitz for the purpose of discussing the April 26 draft contract article.

I stated that the purpose of the draft article was to express in contract language the position we are taking in the tax litigation on the nature of the relationship between ERDA and a management contractor such as Sandia. I pointed out that all of the principles stated in the draft, and much of the exact wording, were lifted from a 1969 law review article by O. S. Hiestand entitled *The AEC Management Contract Concept*, and that paragraph I was taken from AEC's Ninth Semiannual Report to Congress.

Mr. Ross stated that he agreed that the draft article was an accurate statement of existing relationship but thought that much of the wording was inappropriate for contract language and unnecessary as far as any tax issues were concerned. He suggested that since the purpose of the article was to express existing principal-agent relationships, we should confine ourselves to that subject and not attempt to deal with irrelevant matters

such as "master-servant" and "principal-independent contractor." Mr. Ross said that he thought the article should be confined to those aspects of the agency relationship enumerated in paragraph 3 of the April 26 draft. He pointed out that each of the aspects of agency enumerated in paragraph 3 could be shown to be based upon existing provisions of the ERDA-Western contract or established methods of operation under that contract. Mr. Ross said he would have no objection, and thought Western would not object, to a contract article which merely expressed or implied in the contract and established methods of operation.

It was agreed that I would prepare a revision to the article which would expand upon the agency aspects enumerated in paragraph 3 of the April 26 draft, showing the basis for each in existing contract provisions or methods of operation. I don't recall any detailed discussions of possible impact of the proposed article on other aspects of ERDA-Sandia operations at this meeting, although such subjects, identified elsewhere in this memorandum, may have been mentioned in passing. Nor do I recall any specific discussion of the question of amending the contract now versus waiting for the five-year renewal effective October 1, 1978, although that, too, may have been mentioned.

After the meeting described above, I prepared a revised draft of an Article XX which I believe was entitled "Status and Authority of Sandia Corporation as an Agent of ERDA" and which was very similar in form and content to the May 20, 1977, draft, previously furnished to the court. I believe I discussed this draft (mainly editorial matters) with Mr. Williamson in the course of its preparation. I believe this draft consisted solely of the Article XX without preamble or "whereas" clauses. This draft was delivered to Sandia counsel several days prior to our next meeting, which took place in Mr. Ross' office, I believe on May 12, 1977. Those in attendance were Messrs. Ross, Jacobvitz, McNett, Wil-

liamson, and San Hamel. Prior to this meeting, Sandia counsel had prepared their own draft which made certain minor revisions in my draft previously furnished to them.

We first discussed the variations in the ERDA and Sandia drafts. There were only two variations that I now recall. Sandia had added a paragraph 5 consisting of what is now, in substance, the last sentence of Article II ("This article shall not be construed to modify any other provisions of the contract nor shall it create rights or obligations not otherwise provided for in the contract.") I said I thought this point was clear enough from the lead-in language at the beginning of the article preceding the numbered paragraphs, and, furthermore, that if the article were to be added by modifications, the intent of Sandia's proposed paragraph 5 would be reflected in the "whereas" clauses of the modification.

Sandia counsel agreed, but said they felt this idea should be more clearly expressed in the article itself. Mr. Ross said he believed that Western would be more likely to find the article acceptable if it were clear that no change in the actual relationship of the parties was intended. After short discussion, Mr. Jacobvitz and I agreed, but said we thought the provision should be put in an unnumbered paragraph at the end, rather than as a paragraph 5. Sandia counsel agreed.

It was mentioned that the added sentence would make it clear that ERDA and Sandia would continue to look to their contract to define their respective rights and obligations as between each other and not to, e.g., the *American Jurisprudence* article on the law of agency.

The only other variation in ERDA and Sandia drafts that I now recall was regarding the parenthetical words "including but not limited to vendors, subcontractors, and employees," which appeared after the word "obligees" in paragraph 4. The Sandia draft had deleted those words as unnecessary. Sandia felt that such words could be used by Sandia employees to inject ERDA into mat-

ters which should be resolved between employer and employee. I don't recall any specific examples. It was agreed that the word "employees" could not simply be left out because they, too, were "obligees" within the meaning of paragraph 4, and in fact the largest class of obligees paid out of ERDA funds by Sandia. It was therefore agreed to delete the entire parenthetical phrase.

There was some discussion concerning whether words should be added at the end of the article, in substance, that "nothing herein shall affect the employer-employee relationship between Sandia and its employees." The consensus was that since nothing in the article could reasonably be interpreted to affect such relationships, such words were unnecessary.

There was some discussion of the first sentence of paragraph 3 ("rights, benefits and advantages flowing to Sandia"). Sandia counsel pointed out that under some arrangements (e.g., pension plans and insurance), Sandia acquires benefits for the employees personally. After some discussion, it was agreed that such rights and benefits were not rights "flowing to Sandia" but rights "flowing to the employees" and that there was no inconsistency between such special cases and paragraph 3 as written.

After discussion of these matters, it was agreed that revised drafts should be prepared for the consideration of ERDA and Sandia management. It was agreed that if local ERDA and Sandia management approved, the draft modifications could then be sent to Western and to ERDA Headquarters for approval.

There was some discussion as to whether the article should be placed in the contract by an immediate modification of the contract, or delayed until after the District Court's decision in the litigation. It was recognized that there were advantages and disadvantages to either course of action.

It was recognized that if the article were placed in the contract immediately, it might be viewed as a mere

attempt to "bootstrap" our way into a favorable decision. Or it might also be viewed as weakening our case for prior years unless carefully worded to express an agency relationship which had existed in the past. On the other hand, if we delayed, got an unfavored decision, and then put the article into the contract, it would be viewed as an attempt to get a "second bite at the apple" by forcing state and federal governments into another round of litigation with resulting uncertainties and contingencies over another prolonged period of time. Placing the article in the contract now was seen as a more straight-forward way of dealing with the state and with the court, especially since we intended to make it clear that we were not changing the contract or our position in the litigation, but only incorporating into the contract by express language the agency aspects which we have consistently argued, in this and other litigation, have always been implicit in the contractual relationships and conduct of the parties.

I pointed out that defendants were almost finished with their discovery and that it might not be possible to have the modifications approved and executed in time to be placed in the record and considered in the court's decision. I said if we could have them ready in time it might prolong the present litigation for a few months, since defendants would certainly want to conduct some discovery concerning the modifications. However, I said that, in my opinion, it would shorten the controversy in the long run to have all pertinent agreements before the court in the litigation now pending. I said I thought it was in the interest of ERDA, Sandia, the state, and the court to get all issues resolved, once and for all, and to avoid the possibility of another round of litigation.

(The above subject (present versus delayed modifications) was discussed at other times by the various participants named herein. The above summary covers all of the essential points mentioned in all of these discussions, to the best of my recollection.)

It was agreed that the next draft of the contract article would be prepared by me in the format of a present modification to the existing contract and that ERDA counsel would consult with the Justice Department before making any final decision on whether to modify the contract now or wait until after the court's decision. We discussed the "whereas" clauses briefly. It was suggested by someone—I don't recall who—that the modification contain a "whereas" clause to the effect that it was being executed for the purpose of informing third parties (or words to that effect) concerning the nature of the relationship which the parties themselves have always recognized.

After the above meeting, I prepared another draft of a modification, including preamble and "whereas" clauses. I showed this draft to Mr. Williamson and Mr. Ross. Mr. Ross made only one suggestion, as I recall, which I adopted and which dealt with the manner in which the transition from AEC to ERDA should be approached in the "whereas" clauses. Thereafter, the May 20, 1977 draft was prepared.

The May 20, 1977 draft was distributed to ERDA management for comment with Mr. Jacobvitz's May 23, 1977 memo route slip. Mr. Jacobvitz and I discussed the distribution to ERDA management briefly. We agreed that only the Manager, Deputy Manager, and Assistant Manager for Logistics would probably be interested, but that we should send it to all of the Assistant Managers just in case others might have some concerns that we could not foresee. The only substantive coment on the May 20 draft from ERDA management was made by Mr. Leenhouts, Assistant Manager for Logistics, who wondered if the final sentence of the contract article ("shall not be construed to modify" etc.) did not undo all that had been done by the preceding provisions. In discussions with Mr. Leenhouts on May 23, I explained the intent of the last sentence as developed in our earlier discussions with Sandia counsel. Mr. Leenhouts said he

understood and was satisfied with the modification. I said, however, that his question might be one that would occur to others and that for clarity we should add what is now the first sentence of the final unnumbered paragraph of the article ("The purpose of this article is to recognize and express existing relationships.") He said that he was satisfied with my explanation and left it up to me whether the additional sentence was needed. I concluded that the additional sentence was helpful and called Mr. Ross, who agreed. I incorporated the sentence into a revised draft dated May 23, 1977.

It was the May 23 draft, with the additional sentence (and not the May 20 draft as stated in our answers to interrogatories) which was delivered to a representative of the Western Electric legal staff. (Also, delivery to the Western representative occurred on Monday, May 23, rather than on Friday, May 20, as stated in plaintiff's earlier answers to interrogatories.) Mr. Ross advised me that Mr. Sparks and Mr. Howard had approved the May 23 draft before it was delivered to Western.

Sometime prior to May 23, I had advised Mrs. Gerety, Counsel, Los Alamos Area Office, that the contract article was under discussion with Sandia counsel and that if a contract modification were agreed upon we would want to make appropriate adaptations and execute similar modifications for Zia and LACI. On May 23, I prepared a draft modification for the Zia contract which adapted the Western modification to the Zia situation and sent this draft to Mrs. Gerety on May 24, 1977. She subsequently discussed it with Zia counsel and called me on June 1 or 2 to discuss Zia comments and to make a few of her own.

Mrs. Gerety said that Zia management questioned whether there should be an "effective date" for a modification which has as its purpose the recognition of long-standing relationships. Zia representatives had said that the true "effective date" of this modification was April 1, 1946. I told her the point was well taken and that I

saw no reason to have an effective date in this type of contract document. (I subsequently deleted reference to an effective date from drafts prepared on June 8, 1977. After that, however, in discussions with Mr. Ross an arbitrary "effective date" of July 1, 1977, was agreed upon. It was considered standard ERDA and Western practice to have an effective date for contract modifications and this approach was not considered inconsistent with the recognition of existing and past relationships. Mr. Ross and I agreed that the effective date pertains to modifications themselves, not to relationships expressed therein. The same effective date was put in the Zia and LACI modifications for consistency.)

Mrs. Gerety next asked if paragraph 1 should be revised to reflect that Zia's fee became Zia's money upon payment. I said we obviously intended that Zia should become the owner of its fee, but that we could put appropriate words in paragraph 1 to reflect this fact.

Mrs. Gerety asked if paragraph 3 was intended to cover union agreements. I said that I saw no reason why union agreements should not be included within the scope of paragraph 3 as written. She pointed out that unions had in the past made efforts to bring AEC (ERDA) into labor negotiations and that paragraph 3 might give them additional encouragement in that regard. I replied that I didn't see how the language could force ERDA into labor negotiations if it was ERDA policy to stay out, which I understood that it was. I then related to her our discussions with Sandia counsel concerning a possible disclaimer of any effect on employer-employee relationships and our conclusions that such language was unnecessary and why. I said we would give the matter some further thought in light of her comment. (I subsequently mentioned this comment to Mr. Jacobvitz, but I do not recall that anyone pursued the matter beyond that.)

Mrs. Gerety asked about the possible effect of the modification on ERDA's tort liability. I told her that

in my opinion there was no inconsistency between the proposed modification and ERDA's position in Federal Tort Claims Act litigation and that the possibility of impact on tort litigation was so speculative that it did not provide a valid reason for not executing the proposed modification. My conclusions on the tort liability question were based on an analysis set out below. I cannot now recall that I made all of these points in my discussions with Mrs. Gerety, but I did mention all of them at one time or another in my discussions with various ERDA counsel (i.e., Mrs. Gerety, Mr. Jacobvitz, Mr. Cunningham, and Mr. Forst). I may also have mentioned some of these points to Mr. Ross and Mr. Williamson, although I do not recall that ERDA's tort liability was ever a major subject in any of the discussions between ERDA and Sandia counsel concerning these modifications. My analysis of the tort question was as follows:

1. There is no inconsistency between the concepts of "agent" and "independent contractor." The law is very clear that one can be an "agent" for certain specified purposes (i.e., business transactions) and still be an "independent contractor" for tort purposes. For more detail on this point, I referred Mrs. Gerety and others to plaintiff's answers to defendants' interrogatories 8, 9, 98, and 99 filed February 7, 1977.

2. The modifications were entirely consistent with the position ERDA was taking in this case and in other previous and current tax and tort litigation. The modifications merely reflected the existing "business agent" status of the contractors. They did not negate the "independent contractor" defense for cases in which the Government is sued under the Federal Tort Claims Act on the basis of alleged acts of negligence on the part of employees of the contractors in the conduct of day-to-day operations in which ERDA does not exercise direct control.

3. It was acknowledged that use of the word "agent" might cause some persons, who might not otherwise do

so, to bring unfounded suits under the Federal Tort Claims Act. That possibility was not considered a valid objection to the modifications for the following reasons:

a. An actual increase in tort litigation above the present level attributable solely to the language of the modifications was highly speculative.

b. The trend today is to join the Government in tort litigation involving ERDA management contractors, anyway.

c. The "independent contractor" defense in tort cases is not always effective, as illustrated by a recent decision of the 9th Circuit in *McGarry* v. *United States*, 549 F.2d 587 (1976).

d. Where the plaintiff is an employee of the contractor, ERDA can frequently invoke the "exclusive remedy" protection accorded to employers under workmen's compensation statutes.

e. Even when the Government is not sued, ERDA and Department of Justice attorneys are frequently involved in the defense of tort litigation brought against ERDA management contractors.

f. The Government pays for all judgments and litigation costs resulting from tort suits against its contractors, whether or not the Government is named defendant. More Federal Tort Claims Act suits would *not* mean more costs to the Government.

g. The modifications are, after all, an accurate statement of the existing relationships as conceived by the parties, and if unfounded tort litigation is an unavoidable fallout from "telling it like it is," so be it.

Sometime between June 2 and June 8, I talked to Mr. Ross about the status of the modification at Western. He advised me that it would not appear that there would be a problem at Western, but that an individual who would have to approve the modification was out of the country and would not be returning for a week or so. It was agreed that we would proceed to submit the proposed modification to ERDA Headquarters.

In previous discussions between Mr. Jacobvitz and me, it had been agreed that we did not need to ask ERDA Headquarters to "approve" the modifications since we were not changing the contractual relationships but only causing the contract to reflect existing relationships. It was recognized, however, that we should advise ERDA Headquarters of our proposed action and give them the opportunity to raise any objection they might have. I prepared the June 9, 1977, submittal to the General Counsel on that basis.

I was away from my office on vacation from June 10 through June 24, 1977. When I returned, I read Mr. Forst's memorandum of June 15, 1977 (previously furnished to the court) and called him to see if the discussions referred to therein had taken place. He said they had not but would let me know when they did. I believe he asked me at this time about tort liability and that I reiterated my opinion and some or all of the points outlined above in connection with my discussions with Mrs. Gerety. I also talked to Mr. Cunningham at this time and requested that he try to move things along in ERDA Headquarters so that we could get the modifications executed, if that was to be the decision. I related to Mr. Cunningham my earlier discussions with Mr. Forst.

A few days later, I was advised by Mr. Forst and Mr. Cunningham that they had discussed the modifications with Mr. Ragan. The consensus as related to me was that the modifications were appropriate, but that a few of the Chief Counsels for other operations offices should be consulted before the General Counsel's final approval was given. I understand that Mr. Ragan asked Mr. Forst to obtain the views of Mr. Hill, Mr. Combo, and Mr. Hames.

Mr. Forst later advised me that he had discussed the modifications by telephone with the three Chief Counsels named above, that he had read the modifications to them, and obtained their reactions. As best I can recall, the reactions of the three Chief Counsels as passed on to me

by Mr. Forst were: Mr. Hill thought the modifications were a good idea; Mr. Combo said he had no problem with them; and Mr. Hames wondered if the word "management" as used in paragraph 2 wasn't too vague and whether some more specific wording might be employed in that paragraph.

I later discussed the reaction of Mr. Hames with Mr. Ross. We were unable to come up with a better word than "management" for use in paragraph 2. Mr. Ross and I considered it an accurate description of what Sandia does with ERDA property.

At some point after my return from vacation, I asked Mr. Forst about the reaction of Mr. Carretta to the modifications. Mr. Forst said that Mr. Carretta was on leave, that he had not heard from him in specific reference to the June 9 Jacobvitz/Ragan memorandum, but that he did not believe Mr. Carretta would have any problem with the modifications and that he would defer to the attorneys on whether they should be executed. It was subsequently confirmed that Mr. Carretta's position was as stated by Mr. Forst. Mr. Forst later told me that Mr. Carretta may have discussed the modifications with other persons in the Division of Procurement, including Mr. Thomas Davin, but I do not know the substance of those discussions.

Up to this point, I had not discussed the modifications in any detail with attorneys for the U.S. Department of Justice. At some time during the process, I told Mr. Charles E. Stratton of Justice that the modifications were being considered. He expressed agreement with the approach of expressing existing relationships, but I don't recall that we discussed any particular draft or specific language.

On July 6, 1977, I met with Mr. Cunningham and Mr. John J. McCarthy, Tax Division, U.S. Department of Justice, in Mr. McCarthy's office in Washington to discuss the modifications, and specifically, whether they should be executed immediately or not until after the

District Court decision in the litigation. The advantages and disadvantages of each course of action, as summarized above in connection with discussions of the same subject with Sandia counsel, were considered.

Mr. McCarthy stated his opinion that modifications should be executed now, rather than after the District Court's decision. He said he felt that since ERDA was contending that their management contractors were "agents" for the stated purposes that the contracts, as well as our briefs and arguments in the litigation, should reflect that position. He pointed out that, even with the modifications, it would still be necessary to convince the court of the existence of agency relationships based on other provisions of the contracts and methods of operation. Our calling them agents didn't make them so, any more than our *not* calling them agents meant they were not. He said the only real advantage to the Government in the litigation from the modifications would be to show that, whether the contractors are agents or not, it is at least not contrary to ERDA policy to contend that they are and call them that.

I called Mr. Ross in Albuquerque from Mr. McCarthy's office and related to him the opinion of Mr. McCarthy as stated above. Mr. Ross had told me previously that he was going to be discussing the modification with Western's legal staff in New York and wanted to know the Justice Department's position in connection with those discussions.

Mr. Ross later prepared his letter of July 12, 1977, to Western. Mr. Ross showed me the letter in draft before it was sent. I don't recall that I had any substantive comment other than to express agreement with the letter. I do recall suggesting that he not refer to the Western contract as a "GOCO" (Government-owned-contractor-operated) contract. This is DOD terminology and not applicable to AEC/ERDA. I believe I showed Mr. Ross' draft to Mr. Jacobvitz and that he had no comment.

I recall only one change in the modifications that was made after the June 8 drafts and that was deletion of the words "or shall be used" in the first sentence of paragraph 2. This change was made in discussions with Mr. Ross. It was agreed that Western was not required to use any of its property in performance of the contract and in fact did not, but that there was no reason to *prohibit* use of Western property if Western should, for any reason, want to do so in the future.

As best I recall, all of my subsequent discussions of the modifications with ERDA, ERDA contractor, and Department of Justice personnel concerned the mechanics of getting the modifications executed and filed with the court, and not with the substantive provisions.

Execution of the modifications was completed on July 22. I advised Mr. Friedman of them on the following working day, July 25, 1977, and provided him with copies on July 26, 1977. They were filed with the court on July 28, 1977.

/s/ John F. McNett
JOHN F. MCNETT

September 12, 1977

ROBERT T. SCOTT AFFIDAVIT 3/26/76 W/NINE EXHIBITS (R.II)

IN THE UNITED STATES DISTRICT COURT FOR THE DISTRICT OF NEW MEXICO

Civil Action No. 75-418

UNITED STATES OF AMERICA, PLAINTIFF

vs.

STATE OF NEW MEXICO; BUREAU OF REVENUE OF THE STATE OF NEW MEXICO; and FRED L. O'CHESKEY, as Commissioner of Revenue of and for the State of New Mexico, and his successors in office, DEFENDANTS

AFFIDAVIT

ROBERT W. SCOTT, being first duly sworn, deposes and says:

1. I have, since February 1975, been Assistant Manager for Administration of the Albuquerque Operations Office (ALO) of the United States Energy Research and Development Administration (ERDA) (formerly the United States Atomic Energy Commission (AEC)). My previous positions with AEC have been the following: Area Manager of the Sandia Area Office, a field office under ALO in Albuquerque, New Mexico, from June 1973, through February 1975; Director of the Budget Division, ALO, from April 1969 through June 1973; and Director of the Finance Division of the Idaho Operations Office in Idaho Falls, Idaho, from July 1959 through April 1969. In my present position as Assistant Manager for Administration I have responsibility for ERDA activity related to the providing of ERDA funds for the use of ERDA operating contractors, including Sandia Corporation under Contract AT(29-1)-789 (Contract 789), the Zia Company (Zia) under Contract W-17-028-

ROBERT T. SCOTT AFFIDAVIT 3/26/76
W/NINE EXHIBITS (R.II)

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ENG-90 (Contract ENG-90), and Los Alamos Constructors, Inc. (LACI) under Contract AT(29-1)-1357 (Contract 1357). ERDA funds are provided for the operations of these contractors through arrangements commonly referred to as "advanced funding."

2. Through the advanced funding arrangements funds are provided from the United States Treasury, through the Federal Reserve bank, for operations under Contract ENG-90 with Zia, Contract 1357 with LACI, and Contract 789 with Sandia Corporation in the following manner:

a. An account is established at a bank approved by ERDA pursuant to a three-party agreement signed by ERDA, the bank of deposit, and the contractor. Attached hereto as exhibits are bank account agreements currently in effect for the funding operations of Zia under Contract ENG-90 (Exhibit 1), of LACI under Contract 1357 (Exhibit 2), and of Sandia Corporation under Contract 789 (Exhibit 3). Other bank account agreements in effect for these contractors are in the same format and contain the same essential provisions as Exhibits 1, 2, and 3.

b. In accordance with the contracts and the bank account agreements, ERDA is the owner of any balance which may exist in any such account. Zia, LACI, and Sandia Corporation never acquire any right, title or interest in or to any balance which may exist in any such account, other than the right and obligation to make expenditures therefrom for contract operations as provided in their respective contracts.

c. ERDA funds are made available for contract operations under Contract 789 in the following manner: Sandia Corporation prepares and executes a payment voucher. Form TUS 5401, in an amount sufficient to cover drafts drawn on the ERDA bank account during a selected period of time (usually one day) and submits it to the bank of deposit. The bank of deposit credits the ERDA special bank account in the amount shown

on the Form TUS 5401 and forwards the form to the appropriate Federal Reserve bank. The Federal Reserve bank credits the account of the bank of deposit in the amount shown on the Form TUS 5401. A sample of an executed Form TUS 5401 used for this purpose is attached hereto as Exhibit 4. A letter of Credit (Standard Form 1193) issued by ERDA in favor of Sandia Laboratories for deposit to the ERDA bank account is the authority of the Federal Reserve bank to provide funds from the account of the United States Treasury to the credit of the bank of deposit upon receipt of the executed Form TUS 5401. A copy of the Letter of Credit issued by ERDA for this purpose is attached hereto as Exhibit 5.

d. ERDA funds are made available for contract operations under Contract ENG-90 and Contract 1357 in the same manner as described in c. above except that the payment voucher, Form TUS 5401, is prepared and executed by the bank of deposit in appropriate amounts as the drafts drawn by Zia and LACI are presented to the bank of deposit for payment. Attached hereto as exhibits are samples of executed Forms TUS 5401 used for funding the operations of Zia (Exhibit 6) and LACI (Exhibit 7). Also attached are copies of the Letter of Credit (Standard Form 1193) authorizing the Federal Reserve bank to provide funds from the account of the United States Treasury to fund the operations of Zia (Exhibit 8) and LACI (Exhibit 9).

3. All valid obligations incurred by Sandia Corporation, by Zia, and by LACI in performance of their respective ERDA contracts, and in accordance with the terms of the contracts, are treated as ERDA liabilities. ERDA can, and occasionally does, elect to make payment directly to obligees on account of liabilities incurred in contract operations as an alternative to having payment made by the ERDA contractor through the advanced funding system described above.

4. The advanced funding method described in this affidavit is routinely used throughout ERDA, with minor variations, for funding the operations of ERDA facilities by ERDA management contractors. Standard contract language for this purpose was prescribed by AEC Procurement Regulations, 41 CFR § 9-7.5006-23 and 24 (reissued as ERDA Procurement Regulations in 40 Fed. Reg., Number 195, October 7, 1975). The prescribed contract language is used, with minor variations, in the Zia and LACI contracts. The system described in the cited CFR provisions (except for the payment of a fee to the contractor) is also used under the Sandia contract. The ERDA advanced funding system as described in this affidavit and applicable CFR provisions is used without regard to tax consequences. The system simplifies the financial aspects of ERDA research, development and production functions. By providing all of the funds necessary to sustain operations under management contracts, ERDA is able to obtain firms willing to perform ERDA functions for no fee or for a very low fee. The system precludes the need for costly borrowing by private firms and eliminates the substantial risks typically imposed on ordinary cost-plus-fixed-fee contractors of the Government.

/s/ Robert W. Scott
ROBERT W. SCOTT

SUBSCRIBED AND SWORN TO before me this 26th day of March.

/s/ Elizabeth R. Gallegos
ELIZABETH R. GALLEGOS
Notary Public

My Commission Expires
February 27, 1977

EXHIBIT 1

SPECIAL BANK ACCOUNT AGREEMENT 9/6/72 BETWEEN ERDA & ZIA AND THE FIRST NATIONAL BANK OF SANTA FE

APPENDIX C

SPECIAL BANK ACCOUNT AGREEMENT

Agreement entered into this 6th day of September 1972, between the United States of America (hereinafter called the "Government"), represented herein by the United States Atomic Energy Commission (hereinafter called the "Commission"), The Zia Company (hereinafter called "Contractor"), a corporation organized under the laws of the State of New Mexico, and the First National Bank of Santa Fe, a national banking corporation located at Santa Fe, New Mexico, acting through its Los Alamos Branch (hereinafter called the "Bank"), located at Los Alamos, New Mexico,

WITNESSETH THAT:

WHEREAS, on July 1, 1967, the Commission, the Contractor and the Bank entered into a Special Bank Account Agreement regarding the Contractor's General Account and Payroll Account with the Bank, which Agreement has been in force until this date; and

WHEREAS, the parties hereto desire and intend that said Agreement shall be superseded by this Special Bank Account Agreement; and

WHEREAS, under effective date of July 1, 1970, the Commission and the Contractor entered into Modification No. 52 to Contract No. W-17-028-Eng-90 providing for continued advances of Government funds to the Con-

tractor, copy of such advance provisions having been furnished to the Bank; and

* * * * *

WHEREAS, the Commission requires that amounts advanced to the Contractor under said contract or modification be deposited in Special Bank Accounts with a bank designated by the Treasury Department as a depositary and financial agent of the Government (Section 10 of the Act of June 11, 1942, 56 Stat. 356; 12 U.S.C. 265), separate from any of the Contractor's general or other funds; and, the Bank being such a bank, the parties agree to deposit said amounts with the Bank.

NOW THEREFORE, in consideration of the foregoing, and for other good and valuable considerations, it is agreed that:

1. The said Special Bank Accounts shall be designated "The Zia Company, Contract No. W-17-028-Eng-90, United States Atomic Energy Commission Special General Bank Account" and "The Zia Company, Contract No. W-17-028-Eng-90, United States Atomic Energy Commission Special Payroll Bank Account."

2. The Government shall have title to the credit balance in said accounts to secure the return of all advances made to the Contractor, which title shall be superior to any lien or claim of the Bank or others with respect to such accounts.

3. The Bank will be bound by the provisions of said contract relating to the deposit and withdrawal of funds in the above Special Bank Accounts, but shall not be responsible for the application of funds properly withdrawn from said Accounts. After receipt by the Bank of written directions from the Contracting Officer, or from the duly authorized representative of the Contracting Officer or the Manager of the Albuquerque Operations Office of the Commission, the Bank

shall act thereon and shall be under no liability to any party hereto for any action taken in accordance with the said written directions.

4. The Government, or its authorized representatives, shall have access to the books and records maintained by the Bank with respect to such Special Bank Accounts at all reasonable times and for all reasonable purposes, including, without limitation, the inspection or copying of such books and records and any and all memoranda, checks, correspondence or documents appertaining thereto. Except as agreed upon by the Government and the Bank, all books and records pertaining to the Special Bank Accounts in the possession of the Bank relating to the Special Bank Account Agreement shall be preserved by the Bank for a period of three (3) years after final payment under the contract to which the Special Bank Account Agreement pertains or otherwise disposed of in such manner as may be agreed upon by the Government and the Bank.

5. In the event of the service of any writ of attachment, levy of execution, or commencement of garnishment proceedings with respect to the Special Bank Accounts, the Bank will promptly notify the Manager, Los Alamos Area Office, Atomic Energy Commission.

6. The "Equal Opportunity" clause set forth in Federal Procurement Regulations Section 1-12.803-2 is hereby incorporated into this Agreement by reference and applies as fully as if set forth completely herein. "Contractor" as used in said clause shall mean the Bank.

IN WITNESS WHEREOF, the parties hereto have caused this agreement to be executed as of day and year first above written.

UNITED STATES ATOMIC ENERGY COMMISSION

By: /s/ Charles C. Campbell
CHARLES C. CAMPBELL

TITLE: Assistant Manager for Logistics
Albuquerque Operations, USAEC

THE ZIA COMPANY

By: /s/ W. L. Miller
TITLE: Manager

FIRST NATIONAL BANK OF SANTA FE
LOS ALAMOS BRANCH

By: /s/ Howard Irwin
TITLE: Vice President

EXHIBIT 2

SPECIAL BANK ACCOUNT AGREEMENT 7/1/67 BETWEEN AEC, LOS ALAMOS CONTRACTORS, INC. & LOS ALAMOS NATIONAL BANK

SPECIAL BANK ACCOUNT AGREEMENT

Agreement entered into this 1st day of July 1967, between the United States of America (hereinafter called the "Government"), represented herein by the United States Atomic Energy Commission (hereinafter called the "Commission"), Los Alamos Constructors, Inc. (hereinafter called the "Contractor"), a corporation organized under the laws of the State of New Mexico, and Los Alamos National Bank, a banking corporation under the laws of the United States of America (hereinafter called the "Bank"), located at Los Alamos, New Mexico,

WITNESSETH THAT:

WHEREAS, on April 20, 1962, the Commission, the Contractor and the Bank entered into a Special Bank Account Agreement regarding the Contractor's General Account and Payroll Account with the Bank, which Agreement has been in force until this date; and

WHEREAS, the parties hereto desire and intend that said Agreement shall be superseded by this Special Bank Account Agreement; and

WHEREAS, under effective date of July 1, 1967, the Commission and the Contractor entered into Modification No. 39 to Contract No. AT(29-1)-1357 providing for continued advances of Government funds to the Contractor, copy of such advance provisions having been furnished to the Bank; and

WHEREAS, the Commission requires that amounts advanced to the Contractor under said contract or modifi-

cation be deposited in Special Bank Accounts with a bank designated by the Treasury Department as a depositary and financial agent of the Government (Section 10 of the Act of June 11, 1942, 56 Stat. 356; 12 U.S.C. 265), separate from any of the Contractor's general or other funds; and, the Bank being such a bank, the parties agree to deposit said amounts with the Bank.

NOW THEREFORE, in consideration of the foregoing, and for other good and valuable considerations, it is agreed that:

1. The said Special Bank Accounts shall be designated "Los Alamos Constructors, Inc., Contract No. AT(29-1)-1357, United States Atomic Energy Commission Special General Bank Account" and "Los Alamos Constructors, Inc., Contract No. AT(29-1)-1357, United States Atomic Energy Commission Special Payroll Bank Account."

2. The Government shall have title to the credit balance in said accounts to secure the return of all advances made to the Contractor, which title shall be superior to any lien or claim of the Bank or others with respect to such accounts.

3. The Bank will be bound by the provisions of said contract relating to the deposit and withdrawal of funds in the above Special Bank Accounts, but shall not be responsible for the application of funds properly withdrawn from said Accounts. After receipt by the Bank of written directions from the Contracting Officer, or from the duly authorized representative of the Contracting Officer or the Manager of the Albuquerque Operations Office of the Commission, the Bank shall act thereon and shall be under no liability to any party thereto for any action taken in accordance with the said written directions.

4. The Government, or its authorized representatives, shall have access to the books and records maintained

by the Bank with respect to such Special Bank Accounts at all reasonable times and for all reasonable purposes, including, without limitation, the inspection or copying of such books and records and any and all memoranda, checks, correspondence or documents appertaining thereto. Except as agreed upon by the Government and the Bank, all books and records pertaining to the Special Bank Accounts in the possession of the Bank relating to the Special Bank Account Agreement shall be preserved by the Bank for a period of three (3) years after final payment under the contract to which the Special Bank Account Agreement pertains or otherwise disposed of in such manner as may be agreed upon by the Government and the Bank.

5. In the event of the service of any writ of attachment, levy of execution, or commencement of garnishment proceedings with respect to the Special Bank Accounts, the Bank will promptly notify the Manager, Los Alamos Area Office, Atomic Energy Commission.

• • • • •

EXHIBIT 3

LETTER AGREEMENT RE: SPECIAL BANK ACCOUNT 10/28/49 BETWEEN AEC, THE SANDIA CORP. AND THE ALBUQUERQUE NATIONAL BANK

October 28, 1949

Albuquerque National Bank
Albuquerque, New Mexico

Gentlemen,

It is proposed to open an account in your bank under the name "SANDIA CORPORATION, AEC ADVANCED FUNDS UNDER CONTRACT NO. AT-(29-1)-789", which shall be subject to the following terms and conditions:

1. The funds deposited therein shall at all times be the property of the Atomic Energy Commission. Sandia Corporation shall acquire no property right, title or interest in or to such funds other than the right to make expenditures therefrom for the purpose of paying costs of performing the work under said Contract.

2. Your Bank shall be under no liability to the Commission or Sandia Corporation for the withdrawal of any funds from said account by properly endorsed checks either signed by a representative of Sandia Corporation or, if in amounts up to $1,000.00, bearing a facsimile signature of such representative, certified in either case to be so authorized, under the seal of Sandia Corporation.

3. The Commission shall have the right to inspect the books and records of your Bank relating to the account or to request and receive from your Bank any information concerning the account.

4. Your Bank shall, when directed by the Commission, discontinue honoring checks thereafter drawn on the account by Sandia Corporation. The Commission may also direct your Bank to return the Commision all or any portion of the balance then in the account, provided that

your Bank will return such funds to the Commission only by means of a check made payable to the Treasurer of the United States.

5. When your Bank receives directions of the character specified above written on Atomic Energy Commission stationery which appear to have been signed by or at the direction of, or under the authority of the Commission, such directions shall be deemed to have been properly issued by the Commission and your bank shall follow such directions and shall be under no liability to Sandia Corporation for so doing.

6. To secure the funds deposited in said account, your Bank will keep U.S. Bonds on deposit with a Federal Reserve Bank or the U.S. Treasury at all times equal in value to the balance in the account. Such Bonds shall be deposited under a Joint Custody Receipt naming your Bank and the Atomic Energy Commission. Your Bank and the Commission will agree upon procedures to be followed in event it becomes appropriate to increase or decrease the number of bonds deposited by your Bank or to substitute other bonds for the bonds then on deposit.

If the arrangement set forth above and approved by the Atomic Energy Commission is acceptable to you, please return the four attached copies of this letter after so indicating in the space provided below.

SANDIA CORPORATION

By /s/ George A. Landry
GEORGE A. LANDRY
President

APPROVED:

ATOMIC ENERGY COMMISSION

By /s/ C. L. Tyler
CARROLL L. TYLER
Manager
Santa Fe Operations Office

The undersigned Bank has received a copy of this agreement and agrees to handle all funds deposited in said account by Sandia Corporation as above provided.

ALBUQUERQUE NATIONAL BANK

By /s/ C. E. Dinkle
Vice Pres.

Payment Voucher on Letter of Credit No. 89-00-1303

...a 5401-S
(Rev. 12-67)
Dept. of the Treasury
6 TFRM 1000

PAYMENT VOUCHER ON LETTER OF CREDIT
(TO BE COLLECTED AS A NON-CASH ITEM)
The drawer's bank shall be the agent of the drawer for the collection of this instrument and each subsequent collecting commercial bank shall be the subagent of the drawer.

2050505
SERIAL NO.
SYMBOL 17-865

VOUCHER NO.	LETTER OF CREDIT NO.	AGENCY STATION SYMBOL	DATE VOUCHER DRAWN	AMOUNT
3906	89-00-1303	89-00-9713	November 26, 1975	$ 35,000.00

NAME AND ADDRESS OF DRAWER	NAME AND ADDRESS OF DRAWER'S BANK	FEDERAL RESERVE BANK OR BRANCH
Sandia Corporation P. O. Box 5800 Albuquerque, New Mexico	Albuquerque National Bank P. O. Box 1344 Albuquerque, New Mexico	Denver Branch

NAME AND ADDRESS OF U. S. AGENCY
U. S. ERDA
Albuquerque Operations Office
P. O. Box 5400
Albuquerque, New Mexico 87115

I certify that this payment voucher has been drawn in accordance with the terms and conditions of the letter of credit cited and that the amount for which drawn is properly for credit to the account of the drawer at the drawer's bank.

M. J. Snyder — Cashier
(Signature) (Title)
(Countersignature) (Title)

Per authorization of Fiscal Assistant Secretary, Treasury Department debit the general account of the Treasurer of the U. S. and pay to the presenting bank the amount shown above.

FOR FEDERAL RESERVE BANK USE ONLY
NOV 28 1975
(Date Debited) (Authorized Signature)

Government agency.

Exhibit 4

Standard Form 1193
8 TREASURY FRM 1000
Fiscal Service, Bureau of Accounts

ISSUING AGENCY	LETTER OF CREDIT	LETTER OF CREDIT NUMBER
U.S. ENERGY RES. & DEVEL. ADMIN. ALBUQUERQUE OPERATIONS OFFICE P.O. BOX 5400 ALBUQUERQUE, NEW MEXICO 87115	Auth: TREASURY DEPARTMENT CIRCULAR No. 1075, Revised	89-00-1303 AMENDMENT NUMBER 20
AGENCY STATION SYMBOL 89-00-9713	(FOR AGENCY USE)	EFFECTIVE DATE DECEMBER 2, 1975

To: The Federal Reserve Bank,	BRANCH BANK AT
KANSAS CITY, MISSOURI	DENVER, COLORADO

Letter of Credit No. 89-00-1303

In accordance with the authorization of the Fiscal Assistant Secretary, Treasury Department, there is hereby authorized for the account and responsibility of the issuing agency a letter of credit:

IN FAVOR OF	FOR DEPOSIT ONLY TO
SANDIA LABORATORIES ALBUQUERQUE, NEW MEXICO ERDA ADVANCED FUNDS UNDER CONTRACT AT(29-1)-789	ALBUQUERQUE NATIONAL BANK ALBUQUERQUE, NEW MEXICO, AND FIRST NATIONAL BANK ALBUQUERQUE, NEW MEXICO ACCOUNT

AMOUNT AUTHORIZED		PRIOR AUTHORIZATION	THIS CHANGE
$ 2,312,503,121.96	☐ EACH MONTH ☐ EACH QUARTER ☒ WITHOUT TIME LIMIT ☐ _____	$ 2,223,470,121.96	Increase $ 89,033,000.00 Decrease $

☒ The unpaid balance of this letter of credit will remain available until you are advised in writing by the Treasury Department that this letter has been revoked.*

OR

☐ The unpaid balance of this letter of credit is revoked at the end of each period indicated and the full amount reestablished at the beginning of the following period until you are advised in writing by the Treasury Department that this letter has been revoked.

The amount of this letter of credit is hereby certified to be drawn against, upon presentation to you of Form TUS 5401, Payment Voucher on Letter of Credit, by the official(s) of the recipient organization whose signature(s) appear(s) on the Standard Form 1194, Authorized Signature Card for Payment Vouchers on Letter of Credit, attached hereto or previously or subsequently furnished you through the Treasury Department.

The amount of each payment voucher paid by a Federal Reserve Bank or branch to a designated commercial bank for credit to the account of the recipient organization shall constitute payment to the recipient organization by the United States.

I certify to the Treasury Department that the payments authorized herein are correct and proper for payment from the appropriations or funds legally committed and available for the purpose, when paid in accordance with the terms and conditions cited above.

*THIS LETTER OF CREDIT IS IRREVOCABLE TO THE EXTENT THE RECIPIENT ORGANIZATION HAS OBLIGATED FUNDS IN GOOD FAITH THEREUNDER IN EXECUTING THE AUTHORIZED FEDERAL PROGRAM IN ACCORDANCE WITH THE GRANT, CONTRACT, OR OTHER AGREEMENT.

DATE CERTIFIED November 17, 1975

AUTHORIZED CERTIFYING OFFICER

ALFONSO SALAS, CHIEF
REPORTS & ACCTNG ACCOUNTING SECTION

TYPED NAME AND TITLE

☆ GPO: 1968—312-659

1193-102

Exhibit 5

Payment Voucher on Letter
of Credit No. 89-00-1316

FORM TUS 5401
(Rev. 12-67)
Dept. of the Treasury
6 TFRM 1000

PAYMENT VOUCHER ON LETTER OF CREDIT
(TO BE COLLECTED AS A NON-CASH ITEM)

The drawer's bank shall be the agent of the drawer for the collection of this instrument and each subsequent collecting commercial bank shall be the subagent of the drawer.

1858966
SERIAL NO.

SYMBOL 17-865

VOUCHER NO.	LETTER OF CREDIT NO.	AGENCY STATION SYMBOL	DATE VOUCHER DRAWN	AMOUNT
1115	89-00-1316	89-00-9713	11-28-75	$ 133,097.40

NAME AND ADDRESS OF DRAWER	NAME AND ADDRESS OF DRAWER'S BANK	FEDERAL RESERVE BANK OR BRANCH
1st Natl Bk of Santa Fe Los Alamos Branch Los Alamos New Mexico	1st Natl Bank of Santa Fe Los Alamos Branch Los Alamos New Mexico	Denver Branch Federal Reserve Bank of Kansas City Missouri .

NAME AND ADDRESS OF U.S. AGENCY

U.S. E.D.A.
Albuquerque Operations Office
P.O. Box 5400
Albuquerque New Mexico 87115

I certify that this payment voucher has been drawn in accordance with the terms and conditions of the letter of credit cited and that the amount for which drawn is properly for credit to the account of the drawer at the drawer's bank.

(SIGNATURE) — Operations Officer (TITLE)

(COUNTERSIGNATURE) — (TITLE)

Per authorization of Fiscal Assistant Secretary, Treasury Department, debit the general account of the Treasurer of the U. S. and pay to the presenting bank the amount shown above.

FOR FEDERAL RESERVE BANK USE ONLY

NOV 28 1975 (DATE DEBITED) — (AUTHORIZED SIGNATURE)

Exhibit 6

Payment Voucher on Letter of Credit No. 89-00-1317

FORM TUS 5401
(Rev. 12-67)
Dept. of the Treasury
6 TFRM 1000

PAYMENT VOUCHER ON LETTER OF CREDIT
(TO BE COLLECTED AS A NON-CASH ITEM)

The drawer's bank shall be the agent of the drawer for the collection of this instrument and each subsequent collecting commercial bank shall be the subagent of the drawer.

1858982
SERIAL NO.

SYMBOL 17-865

VOUCHER NO.	LETTER OF CREDIT NO.	AGENCY STATION SYMBOL	DATE VOUCHER DRAWN	AMOUNT
665	89-00-1317	89-00-9713	5 DEC 75	$ 17,409.28

NAME AND ADDRESS OF DRAWER	NAME AND ADDRESS OF DRAWER'S BANK	FEDERAL RESERVE BANK OR BRANCH
1st Nat'l Bank of Santa Fe Los Alamos Branch Los Alamos, New Mexico	1st Nat'l Bank of Santa Fe Los Alamos Branch Los Alamos, New Mexico	Denver Branch Federal Reserve Bank of Kansas City, Missouri

NAME AND ADDRESS OF U.S. AGENCY
U.S. E.R.D.A.
Albuquerque Operations Office
P.O. Box 5400
Albuquerque, New Mexico 87115

I certify that this payment voucher has been drawn in accordance with the terms and conditions of the letter of credit cited and that the amount for which drawn is properly for credit to the account of the drawer at the drawer's bank.

(SIGNATURE) — Operations Officer (TITLE)

(COUNTERSIGNATURE) — (TITLE)

Per authorization of Fiscal Assistant Secretary, Treasury Department, debit the general account of the Treasurer of the U. S. and pay to the presenting bank the amount shown above.

FOR FEDERAL RESERVE BANK USE ONLY

(DATE DEBITED) — (AUTHORIZED SIGNATURE)

Exhibit 7

8 TREASURY FRM 1000
Fiscal Service, Bureau of Accounts

ISSUING AGENCY	LETTER OF CREDIT	LETTER OF CREDIT NUMBER
U.S. ERDA ALBUQUERQUE OPERATIONS OFFICE P.O. BOX 5400 ALBUQUERQUE, N. M. 87115	Auth: TREASURY DEPARTMENT CIRCULAR No. 1075, Revised	89-00-1316 AMENDMENT NUMBER 22
AGENCY STATION SYMBOL 89-00-9713	(FOR AGENCY USE)	EFFECTIVE DATE DECEMBER 17, 1975

TO: The Federal Reserve Bank,	BRANCH BANK AT
KANSAS CITY, MISSOURI	DENVER, COLORADO Letter of Credit No 89-00-1316

In accordance with the authorization of the Fiscal Assistant Secretary, Treasury Department, there is hereby authorized for the account and responsibility of the issuing agency a letter of credit:

IN FAVOR OF	FOR DEPOSIT ONLY TO
FIRST NATIONAL BANK OF SANTA FE LOS ALAMOS BRANCH LOS ALAMOS, N.M. 87544	THE ZIA COMPANY CONTRACT W-17-023-ENG-90 U.S. ERDA ACCOUNT

AMOUNT AUTHORIZED		PRIOR AUTHORIZATION	THIS CHANGE
$ 72,413,022.41	☐ EACH MONTH ☐ EACH QUARTER ☒ WITHOUT TIME LIMIT ☐ _____	$ 68,740,311.41	Increase $ 3,672,711.00 Decrease $ -

☒ The unpaid balance of this letter of credit will remain available until you are advised in writing by the Treasury Department that this letter has been revoked.

OR

☐ The unpaid balance of this letter of credit is revoked at the end of each period indicated and the full amount reestablished at the beginning of the following period until you are advised in writing by the Treasury Department that this letter has been revoked.

The amount of this letter of credit is hereby certified to be drawn against, upon presentation to you of Form TUS 5401, Payment Voucher on Letter of Credit, by the official(s) of the recipient organization whose signature(s) appear(s) on the Standard Form 1194, Authorized Signature Card for Payment Vouchers on Letter of Credit, attached hereto or previously or subsequently furnished you through the Treasury Department.

The amount of each payment voucher paid by a Federal Reserve Bank or branch to a designated commercial bank for credit to the account of the recipient organization shall constitute payment to the recipient organization by the United States.

I certify to the Treasury Department that the payments authorized herein are correct and proper for payment from the appropriations or funds legally committed and available for the purpose, when paid in accordance with the terms and conditions cited above.

*THIS LETTER OF CREDIT IS IRREVOCABLE TO THE EXTENT THE RECIPIENT ORGANIZATION HAS OBLIGATED FUNDS IN GOOD FAITH THEREUNDER IN EXECUTING THE AUTHORIZED FEDERAL PROGRAM IN ACCORDANCE WITH THE GRANT, CONTRACT, OR OTHER AGREEMENT.

DATE CERTIFIED DECEMBER 8, 1975

Alfonso Salas
AUTHORIZED CERTIFYING OFFICER
ALFONSO SALAS, CHIEF
REPORTS AND MACHINE ACCOUNTING SECTION
TYPED NAME AND TITLE

☆ GPO: 1968—319-859

Exhibit 8

Standard Form 1193
I TREASURY FRM 1000
Fiscal Service, Bureau of Accounts

ISSUING AGENCY	LETTER OF CREDIT	LETTER OF CREDIT NUMBER
U.S. ERDA ALBUQUERQUE OPERATIONS OFFICE P.O. BOX 5400 ALBUQUERQUE, NM 87115	Auth: TREASURY DEPARTMENT CIRCULAR No. 1075, Revised	89-00-1317 AMENDMENT NUMBER 16
AGENCY STATION SYMBOL 89-00-9713	(FOR AGENCY USE)	EFFECTIVE DATE DECEMBER 22, 1975

To: The Federal Reserve Bank,	BRANCH BANK AT
KANSAS CITY, MISSOURI	DENVER, COLORADO Letter of Credit No. 89-00-1317

In accordance with the authorization of the Fiscal Assistant Secretary, Treasury Department, there is hereby authorized for the account and responsibility of the issuing agency a letter of credit:

IN FAVOR OF	FOR DEPOSIT ONLY TO
FIRST NATIONAL BANK OF SANTA FE LOS ALAMOS BRANCH LOS ALAMOS, NM 87544	LOS ALAMOS CONSTRUCTORS, INC. CONTRACT AT(29-1)-1357 U.S. ENERGY RES. & DEVEL. ADMIN. ACCOUNT

AMOUNT AUTHORIZED		PRIOR AUTHORIZATION	THIS CHANGE
$ 6,820,285.07	☐ EACH MONTH ☐ EACH QUARTER ☒ WITHOUT TIME LIMIT ☐ _____	$ 6,595,285.07	Increase $225,000.00 Decrease $

☒ The unpaid balance of this letter of credit will remain available until you are advised in writing by the Treasury Department that this letter has been revoked.

OR

☐ The unpaid balance of this letter of credit is revoked at the end of each period indicated and the full amount reestablished at the beginning of the following period until you are advised in writing by the Treasury Department that this letter has been revoked.

The amount of this letter of credit is hereby certified to be drawn against, upon presentation to you of Form TUS 5401, Payment Voucher on Letter of Credit, by the official(s) of the recipient organization whose signature(s) appear(s) on the Standard Form 1194, Authorized Signature Card for Payment Vouchers on Letter of Credit, attached hereto or previously or subsequently furnished you through the Treasury Department.

The amount of each payment voucher paid by a Federal Reserve Bank or branch to a designated commercial bank for credit to the account of the recipient organization shall constitute payment to the recipient organization by the United States.

I certify to the Treasury Department that the payments authorized herein are correct and proper for payment from the appropriations or funds legally committed and available for the purpose, when paid in accordance with the terms and conditions cited above.

"THIS LETTER OF CREDIT IS IRREVOCABLE TO THE EXTENT THE RECIPIENT ORGANIZATION HAS OBLIGATED FUNDS IN GOOD FAITH THEREUNDER IN EXECUTING THE AUTHORIZED FEDERAL PROGRAM IN ACCORDANCE WITH THE GRANT, CONTRACT, OR OTHER AGREEMENT.

DATE CERTIFIED DECEMBER 10, 1975

Alfonso Salas
AUTHORIZED CERTIFYING OFFICER

ALFONSO SALAS, CHIEF
REPORTS & VOUCHER ACCOUNTING SECTION
TYPED NAME AND TITLE

☆ GPO: 1968—319-059

1193-105

Exhibit 9

Ex 17 - Ex. 18

SANDIA CORPORATION
SANDIA BASE
ALBUQUERQUE, NEW MEXICO

TO FIRST NATIONAL BANK IN ALBUQUERQUE
ALBUQUERQUE, NEW MEXICO

95-1
1022

CODE 02 CHECK NO. 41399 DATE 10/15/75 PAY $**755.00 C

(SURNAME FIRST)

08115 OVER $1000* NOT VALID

[NAME DELETED]

SANDIA CORPORATION

CANCELLED

(SURNAME FIRST)

PAYABLE IF DESIRED AT WELLS FARGO LIVER
MORE , CALORNIA, 90-410/

216776 ⑆1022⑈000⑆ 100 000 202⑈

SANDIA CORPORATION
SANDIA BASE
ALBUQUERQUE, NEW MEXICO

TO FIRST NATIONAL BANK IN ALBUQUERQUE
ALBUQUERQUE, NEW MEXICO

95-1
1022

CHECK NO. 73216 DATE 02/03/75 PAY$******38.0

THE OPTICAL PUBLISHING CO INC
LENOX ROAD
PITTSFIELD MA 01201

SANDIA CORPORATION

CANCELLED

MENT OF THE ITEMS LISTED ON THE ACCOMPANYING REMITTANCE ADVICE.

,38359 ⑆1022⑈000⑆ 100 000 202⑈

SANDIA CORPORATION
SANDIA BASE
ALBUQUERQUE, NEW MEXICO

TO ALBUQUERQUE NATIONAL BANK
ALBUQUERQUE, NEW MEXICO

95-8
1022

CODE 02 CHECK NO. 18795 DATE 1/31/75 PAY $***146.70

(SURNAME FIRST)

08256 OVER $500** NOT VALID

[NAME DELETED]

SANDIA CORPORATION

CANCELLED

(SURNAME FIRST)

PAYABLE IF DESIRED AT WELLS FARGO BANK
LIVERMORE, CALIFORNIA, 90-410

192015 :1022=0008: 00 0286 0=

SANDIA CORPORATION
SANDIA BASE
ALBUQUERQUE, NEW MEXICO

TO ALBUQUERQUE NATIONAL BANK
ALBUQUERQUE, NEW MEXICO

95-8
1022

CHECK NO. 71288 DATE 02/13/75 PAY$ *****120.00

PLENUM PUBL CO
227 WEST 17TH ST
NEW YORK NY 10011

SANDIA CORPORATION

CANCELLED

YMENT OF THE ITEMS LISTED ON THE ACCOMPANYING REMITTANCE ADVICE.

LOS ALAMOS CONSTRUCTORS, INC.
GENERAL ACCOUNT
LOS ALAMOS, NEW MEXICO 87544

Ex. 19

1-3 1975

25-191
1022

REGISTERED RD-246 2902 dollars 77 cts

PAY DOLLARS $ 2,902.77

TO THE ORDER OF

The First National Bank of Santa Fe
Los Alamos Branch

Void

LOS ALAMOS CONSTRUCTORS, INC.

C. D. Tyson

B. W. Bain

LOS ALAMOS BRANCH
THE FIRST NATIONAL BANK OF SANTA FE LOS ALAMOS, NEW MEXICO
THE OLDEST BANK IN THE SOUTHWEST

⑈1022⑈0191⑈ 59 0012 3⑈ ⑈0000290277⑈

t 116

THE ZIA COMPANY, LOS ALAMOS, NEW MEXICO 095788

AEC ADVANCED FUNDS

95-191
1022

JUN 26 1975

REGISTERED RD-246 289 dollars 60 cts

AMOUNT
$ 289.60

THE ZIA COMPANY

NOT TO EXCEED $1,000.

Void

PAY TO THE ORDER OF C. W. Ketchell

FIRST NATIONAL BANK OF SANTA FE
LOS ALAMOS BRANCH
LOS ALAMOS, NEW MEXICO

⑈1022⑈0191⑈ 59 0006 9⑈ ⑈0000028960

A.E.C. ADVANCED FUNDS
PAYROLL ACCOUNT
NOT TO EXCEED $500

PAY TO THE ORDER OF

THE ZIA COMPANY
LOS ALAMOS, NEW MEXICO

Void

[NAME DELETED]

*119 DOLLARS .97 CENTS

08 31 75 623

$119.97

THE ZIA COMPANY

L. D. Tyson

P. L. Miller

2-2 C4561

IRONS OR ERASURES OF NAME
OUNT INVALIDATES THIS CHECK
AID UNLESS CASHED WITHIN 90 DAYS

FIRST NATIONAL BANK OF SANTA FE
LOS ALAMOS BRANCH
LOS ALAMOS, NEW MEXICO

⑈250648⑈ ⑆1070⑈0044⑆ 59 0007 7⑈ ⑈0000011997

66

EX.20

EX.20

Sandia Laboratories
Albuquerque, New Mexico 87115
OPERATED BY SANDIA CORPORATION
for
ENERGY RESEARCH AND DEVELOPMENT ADMINISTRATION
ADVANCE FUNDS ACCOUNT - CONTRACT (29-1)-789

TO FIRST NATIONAL BANK IN ALBUQUERQUE
ALBUQUERQUE, NEW MEXICO

95-27
1070

CODE CHECK NO. DATE / /

PAY $

(SURNAME FIRST)

OVER $_____ NOT VALID

SANDIA CORPORATION

CANCELLED

SA 9424-EF(3-78)

0002 ⑈1070⑈002 7⑈ 100 000 20 2⑈

Sandia Laboratories
Albuquerque, New Mexico 87115
OPERATED BY SANDIA CORPORATION
for
ENERGY RESEARCH AND DEVELOPMENT ADMINISTRATION
ADVANCE FUNDS ACCOUNT - CONTRACT (29-1)-789

TO FIRST NATIONAL BANK IN ALBUQUERQUE
ALBUQUERQUE, NEW MEXICO

95-27
1070

CHECK NO. DATE / /

PAY $

SANDIA CORPORATION

CANCELLED

MENT OF THE ITEMS LISTED ON THE ACCOMPANYING REMITTANCE ADVICE

SA 9424-A2(

0002 ⑈1070⑈002 7⑈ 100 000 20 2⑈

Sandia Laboratories
Albuquerque, New Mexico 87115
OPERATED BY SANDIA CORPORATION
for
ENERGY RESEARCH AND DEVELOPMENT ADMINISTRATION
ADVANCE FUNDS ACCOUNT - CONTRACT (29-1)-789

TO ALBUQUERQUE NATIONAL BANK
ALBUQUERQUE, NEW MEXICO

95-32
1070

CODE CHECK NO. DATE / /

PAY $

(SURNAME FIRST)

OVER $_____ NOT VALID

SANDIA CORPORATION

CANCELLED

SA9424-EA(3-78)

0002 ⑈1070⑈002 7⑈ 100 000 20 2⑈

EX. 21

TAB STOP TAB STOP

THE ZIA COMPA Y, LOS ALAMOS, NEW MEXICO 16949

C TRACT W-17-025-ENG-90
U.S. ENERGY RESI RCH AND DEVELOPMENT ADMINISTRATION
DVANCE FUNDS ACCOUNT

THE FIRST NATIONAL BANK OF SANTA FE 93-87
LOS ALAMOS BRANCH 1070
LOS ALAMOS, NEW MEXICO

AMOUNT
$

Y
THE
DER OF: Void

THE ZIA COMPANY

BY: Void

BY:

⑆1070⑈0083⑆ 59 0006 9⑈

ZIA COMPANY, LOS ALAMOS, NEW MEXICO
CONTRACT W - 17 - 025 - ENG - 90
ERGY RESEARCH AND DEVELOPMENT ADMINISTRATION
ADVANCE FUNDS ACCOUNT

PAY TO THE
ORDER OF

THE ZIA COMPANY
LOS ALAMOS, NEW MEXICO

HELIGENDRO APODACA Void

08	22	76	671

$223.57

*223 DOLLARS .57 CENTS

THE ZIA COMPANY

-9 81862

ONS OR ERASURES OF NAME
JNT INVALIDATES THIS CHECK
JD UNLESS CASHED WITHIN 90 DAYS

FIRST NATIONAL BANK OF SANTA FE
LOS ALAMOS BRANCH
LOS ALAMOS, NEW MEXICO

⑈3127421⑈ ⑆1070⑈0083⑆ 59 0007 7⑈

1002

Plaintiff's Answer to
Defendants' Interrogatory
116 and Exhibits 18-21,
filed August 31, 1976
(R.IV)

116. State all written material contained on checks issued by Zia, LACI, and Sandia to their respective suppliers. Attach samples of such checks issued in 1975 both for payroll and outside supplier payments, and more than one sample of each if different types of checks were used, if you will do so without a request for production. If you do not attach copies, state where such checks may be inspected by defendants.

ANSWER: In response to this interrogatory, the following Exhibits are attached hereto:

- Exhibit 18: Sample checks used by Sandia in FY 1975

Exhibit 19: Sample checks used by Zia and LACI in FY 1975

Exhibit 20: Sample checks currently in use by Sandia

Exhibit 21: Sample checks currently in use by Zia

Checks currently in use by LACI are the same as Exhibit 19.

1004

Item 44(8)

Ex 17 - Ex. 18

SANDIA CORPORATION
SANDIA BASE
ALBUQUERQUE, NEW MEXICO

TO FIRST NATIONAL BANK IN ALBUQUERQUE
ALBUQUERQUE, NEW MEXICO

95-1
1022

CODE 02 CHECK NO. 41399 DATE 10/15/75 PAY $**755.00 CT

(SURNAME FIRST)

08115

OVER $1000* NOT VALID

[NAME DELETED]

(SURNAME FIRST)

SANDIA CORPORATION

CANCELLED

SC 9424-EP (7-63)

PAYABLE IF DESIRED AT WELLS FARGO LIVER
MORE , CALORNIA, 90-410/

216776 ⑈1022⑈000⑆ 100 000 20 2⑈

SANDIA CORPORATION
SANDIA BASE
ALBUQUERQUE, NEW MEXICO

TO FIRST NATIONAL BANK IN ALBUQUERQUE
ALBUQUERQUE, NEW MEXICO

95-1
1022

CHECK NO. 73216 DATE 02/03/75 PAY$******38.0

THE OPTICAL PUBLISHING CO INC
LENOX ROAD
PITTSFIELD MA 01201

SANDIA CORPORATION

CANCELLED

SC 9424-A2 (7-63)

YMENT OF THE ITEMS LISTED ON THE ACCOMPANYING REMITTANCE ADVICE.

,38359 ⑈1022⑈000⑆ 100 000 20 2⑈

226

SANDIA CORPORATION
SANDIA BASE
ALBUQUERQUE, NEW MEXICO

TO ALBUQUERQUE NATIONAL BANK
ALBUQUERQUE, NEW MEXICO

95-8
1022

CODE 02 CHECK NO. 18795 DATE 1/31/75 PAY $***146.70C

(SURNAME FIRST)

TO THE ORDER OF [NAME DELETED]

08256

OVER $500** NOT VALID

SANDIA CORPORATION

CANCELLED

SC 9424-EA (1-65)

PAYABLE IF DESIRED AT WELLS FARGO BANK
LIVERMORE, CALIFORNIA, 90-410

192015 :1022:0008: 00 0286 0

SANDIA CORPORATION
SANDIA BASE
ALBUQUERQUE, NEW MEXICO

TO ALBUQUERQUE NATIONAL BANK
ALBUQUERQUE, NEW MEXICO

95-8
1022

CHECK NO. 71288 DATE 02/13/75 PAY$ *****120.00C

TO THE ORDER OF PLENUM PUBL CO
227 WEST 17TH ST
NEW YORK NY 10011

SANDIA CORPORATION

CANCELLED

SC 9424-A1

YMENT OF THE ITEMS LISTED ON THE ACCOMPANYING REMITTANCE ADVICE.

GENERAL ACCOUNT
LOS ALAMOS, NEW MEXICO 87544

105

Ex. 19

1-3 1975

95-191
1022

REGISTERED RD-246 2902 dollars 77 cents

PAY DOLLARS $ 2,902.77

TO THE ORDER

The First National Bank of Santa Fe
Los Alamos Branch

Void

LOS ALAMOS CONSTRUCTORS, INC.

L. D. Lyons

B. W. Burn

LOS ALAMOS BRANCH
THE FIRST NATIONAL BANK OF SANTA FE LOS ALAMOS, NEW MEXICO

⑆1022⑆0191⑆ 59 0012 3⑈ "0000290277"

I 116

THE ZIA COMPANY, LOS ALAMOS, NEW MEXICO

095788

95-191
1022

AEC ADVANCED FUNDS

JUN 26 1975

REGISTERED RD-246 289 dollars 60 cents

AMOUNT
$ 289.60

THE ZIA COMPANY

PAY THE ORDER OF C. W. Ketchell

Void

NOT TO EXCEED $1,000.

FIRST NATIONAL BANK OF SANTA FE
LOS ALAMOS BRANCH
LOS ALAMOS, NEW MEXICO

⑆1022⑆0191⑆ 59 0006 9⑈ "00000289 60"

95-10

A.E.C. ADVANCED FUNDS
PAYROLL ACCOUNT
NOT TO EXCEED $500

THE ZIA COMPANY
LOS ALAMOS, NEW MEXICO

Void

08 31 75 62334

$119.97

PAY TO THE ORDER OF

[NAME DELETED]

*119 DOLLARS .97 CENTS

THE ZIA COMPANY

L. D. Lyons

W. Mellon

22-2 C4561

ATIONS OR ERASURES OF NAME
AUD UNLESS CASHED WITHIN 90 DAYS

FIRST NATIONAL BANK OF SANTA FE
LOS ALAMOS BRANCH
LOS ALAMOS, NEW MEXICO

⑈250648⑈ ⑆1070⑆0044⑆ 59 0007 7⑈ "00000 11997"

105

EX 120

106

EX. 20

100

Sandia Laboratories
Albuquerque, New Mexico 87115
OPERATED BY SANDIA CORPORATION
for
ENERGY RESEARCH AND DEVELOPMENT ADMINISTRATION
ADVANCE FUNDS ACCOUNT - CONTRACT (29-1)-789

TO FIRST NATIONAL BANK IN ALBUQUERQUE
ALBUQUERQUE, NEW MEXICO

95-27
1070

CODE CHECK NO. DATE / /

PAY $ CTS

(SURNAME FIRST)

OVER $_____ NOT VALID

SANDIA CORPORATION

CANCELLED

SA 9424-EF(3-76)

(SURNAME FIRST)

0002 ⑆1070⑆0027⑆ 100 000 20 2⑈

Sandia Laboratories
Albuquerque, New Mexico 87115
OPERATED BY SANDIA CORPORATION
for
ENERGY RESEARCH AND DEVELOPMENT ADMINISTRATION
ADVANCE FUNDS ACCOUNT - CONTRACT (29-1)-789

TO FIRST NATIONAL BANK IN ALBUQUERQUE
ALBUQUERQUE, NEW MEXICO

95-27
1070

CHECK NO. DATE / /

PAY $ CT

SANDIA CORPORATION

CANCELLED

YMENT OF THE ITEMS LISTED ON THE ACCOMPANYING REMITTANCE ADVICE

SA 9424-AE(

0002 ⑆1070⑆0027⑆ 100 000 20 2⑈

Sandia Laboratories
Albuquerque, New Mexico 87115
OPERATED BY SANDIA CORPORATION
for
ENERGY RESEARCH AND DEVELOPMENT ADMINISTRATION
ADVANCE FUNDS ACCOUNT - CONTRACT (29-1)-789

TO ALBUQUERQUE NATIONAL BANK
ALBUQUERQUE, NEW MEXICO

95-32
1070

CODE CHECK NO. DATE / /

PAY $ CT

(SURNAME FIRST)

OVER $_____ NOT VALID

SANDIA CORPORATION

CANCELLED

SA9424-EA(3-76)

(SURNAME FIRST)

0002 ⑆1070⑆0032⑆ 00 0382 0⑈

106

229

EX. 21

1007

TAB STOP TAB STOP

16949

THE ZIA COMPANY, LOS ALAMOS, NEW MEXICO
CONTRACT W-17-028-ENG-90
U.S. ENERGY RESEARCH AND DEVELOPMENT ADMINISTRATION
ADVANCE FUNDS ACCOUNT

THE FIRST NATIONAL BANK OF SANTA FE
LOS ALAMOS BRANCH
LOS ALAMOS, NEW MEXICO
85-83
1070

AMOUNT
$

THE ZIA COMPANY

PAY
TO THE
ORDER OF

Void

BY: Void

BY:

⑈1070⑈0083⑈ 59 0006 9⑈

ZIA COMPANY, LOS ALAMOS, NEW MEXICO
CONTRACT W-17-028-ENG-90
ENERGY RESEARCH AND DEVELOPMENT ADMINISTRATION
ADVANCE FUNDS ACCOUNT

85-1
107

THE ZIA COMPANY
LOS ALAMOS, NEW MEXICO

PAY TO THE
ORDER OF

Void

HELIGENDRO F MPUDIA

08	22	76	67187

$223.57

*223 DOLLARS •57 CENTS

THE ZIA COMPANY

2-9 81862

TIONS OR ERASURES OF NAME
OUNT INVALIDATES THIS CHECK
AID UNLESS CASHED WITHIN 90 DAYS

E FIRST NATIONAL BANK OF SANTA FE
LOS ALAMOS BRANCH
LOS ALAMOS, NEW MEXICO

⑈311274 2⑈ ⑆1070⑈0083⑆ 59 0007 7⑈

STIPULATION REGARDING THE TESTIMONY OF W. C. STEIN WITH ONE EXHIBIT
(R.I. pp. 141-145)

IN THE UNITED STATES DISTRICT COURT FOR THE DISTRICT OF NEW MEXICO

Civil No. 75-413

UNITED STATES OF AMERICA, PLAINTIFF

vs.

STATE OF NEW MEXICO, ET AL., DEFENDANTS

STIPULATION

The parties, by their respective attorneys, stipulate that a deposition of Mr. W. C. Stein, Senior Vice President and Cashier, First National Bank in Albuquerque would state the following facts:

1. A portion of the "advanced funds" (i.e., funds provided pursuant to 31 C.F.R. Part 205) utilized by Sandia Laboratories are provided through Bank Account No. 100-000-202 at the First National Bank in Albuquerque, hereinafter referred to as the "bank".

2. Consistent with the procedures described in the March 24, 1977, affidavit of Robert W. Scott, a Sandia employee completes Treasury Form TUS 5401 on each work day in the amount of the checks drawn by Sandia that day. On the following day the Sandia employee telephones the bank to provide the TUS 5401 number and amount which the bank is authorized to withdraw against the letter of credit. The bank then teletypes a request for the funds to the Federal Reserve Bank in Denver at which time the requested funds are credited to the bank's account at the Federal Reserve Bank. Upon receipt of the credit at the Federal Reserve Bank, the bank simultaneously enters the proceeds as a deposit to Bank Account No. 100-000-202 where the funds remain until the related Sandia checks clear for payment.

3. The reason for this one-day delay is to reduce insofar as possible the time that the funds are in the account before they are drawn on as payees put their checks through for payment. As a consequence, the balance in the account at any particular time tends to be quite low.

4. The bank maintains with respect to Account No. 100-000-202, the customary records which are maintained with respect to any other checking account. In addition, the bank maintains with respect to said account a copy of an agreement attached hereto as Exhibit 1. Exhibit 1 is the only record maintained by the bank with respect to said account which is different from records kept for any other checking account.

5. All the persons empowered to write checks drawn on the named account are Sandia employees.

6. Any monthly statements of account which the bank prepares are routinely sent to Sandia.

7. The bank has not to date received any directives from ERDA or its predecessor, the Atomic Energy Commission, requiring it to make some special disposition of the funds in the account utilized by Sandia. To date all withdrawals from the account have been upon submission of checks drawn by Sandia employees.

JOHN J. MCCARTHY
Chief, General Litigation Section
Tax Division
U.S. Department of Justice
Washington, D.C. 20530

By Daniel H. Friedman
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VICTOR R. ORTEGA
United States Attorney
Post Office Box 607
Albuquerque, New Mexico 87103

By Ruth C. Streeter
RUTH C. STREETER
First Assistant United States Attorney

EXHIBIT 1

October 28, 1949

First National Bank
in Albuquerque
Albuquerque, New Mexico

Gentlemen:

It is proposed to open an account in your Bank under the name "SANDIA CORPORATION, AEC ADVANCED FUNDS UNDER CONTRACT NO. AT-(29-1)-789", which shall be subject to the following terms and conditions:

1. The funds deposited therein shall at all times be the property of the Atomic Energy Commission. Sandia Corporation shall acquire no property right, title or interest in or to such funds other than the right to make expenditures therefrom for the purpose of paying costs of performing the work under said Contract.

2. Your Bank shall be under no liability to the Commission or Sandia Corporation for the withdrawal of any funds from said account by properly endorsed checks either signed by a representative of Sandia Corporation or, if in amounts up to $1,000.00, bearing a facsimile signature of such representative, certified in either case to be so authorized, under the seal of Sandia Corporation.

3. The Commission shall have the right to inspect the books and records of your Bank relating to the account or to request and receive from your Bank any information concerning the account.

4. Your Bank shall, when directed by the Commission, discontinue honoring checks thereafter drawn on the account by Sandia Corporation. The Commission may also direct your Bank to return to the Commission

all or any portion of the balance then in the account, provided that your Bank will return such funds to the Commission only by means of a check made payable to the Treasurer of the United States.

5. When your Bank receives directions of the character specified above written on Atomic Energy Commission stationery which appear to have been signed by or at the direction of, or under the authority of the Commission, such directions shall be deemed to have been properly issued by the Commission and your Bank shall follow such directions and shall be under no liability to Sandia Corporation for so doing.

6. To secure the funds deposited in said account, your Bank will keep U.S. Bonds on deposit with a Federal Reserve Bank or the U.S. Treasury at all times equal in value to the balance in the account. Such Bonds shall be deposited under a Joint Custody Receipt naming your Bank and the Atomic Energy Commission. Your Bank and the Commission will agree upon procedures to be followed in event it becomes appropriate to increase or decrease the number of bonds deposited in your Bank or to substitute other bonds for the bonds then on deposit.

If the arrangement set forth above and approved by the Atomic Energy Commission is acceptable to you, please return the four attached copies of this letter after so indicating in the space provided below.

SANDIA CORPORATION

By /s/ George A. Landry
GEORGE A. LANDRY
President

APPROVED:

ATOMIC ENERGY COMMISSION

By /s/ Carroll L. Tyler
CARROLL L. TYLER
Manager
Santa Fe Operations Office

The undersigned Bank has received a copy of this agreement and agrees to handle all funds deposited in said account by Sandia Corporation as above provided.

FIRST NATIONAL BANK
IN ALBUQUERQUE
By /s/ [Illegible]

ERNEST CUARON AFFIDAVIT, WITH TWO EXHIBITS, 8/6/77 EXHIBIT 1 TO DEFENDANTS' CROSS-MOTION FOR SUMMARY JUDGMENT (R.III)

IN THE UNITED STATES DISTRICT COURT FOR THE DISTRICT OF NEW MEXICO

Civil Action No. 75-418

UNITED STATES OF AMERICA, PLAINTIFF

vs.

STATE OF NEW MEXICO, ET AL., DEFENDANTS

AFFIDAVIT

Ernest Cuaron being duly sworn deposes and says:

1. I am the Controller of New Mexico Professional Standards Review Organization, Inc., (hereinafter "the corporation") a not-for-profit corporation organized in 1971 under the laws of New Mexico, and located at 2650 Yale Boulevard, S.E., Albuquerque, New Mexico.

2. The corporation performs a contract for the United States Department of Health, Education and Welfare under which it reviews admissions of Title XIX, XVIII and V patients into a New Mexico hospital or institution and the length of stay of such patients, to see if they are justified by medical necessity. This function protects against unnecessary expenditures under federal medical assistance programs.

3. Up to July 1, 1977, the funds for operation of the corporation were obtained from the Department of Health, Education and Welfare by submission of monthly vouchers to obtain reimbursements for expenditures already made.

4. Beginning August 1, 1977, the corporation has begun to receive its funds pursuant to Federal Letter of

Credit No. 75-08-M786, attached hereto as Exhibit A, which funds are deposited in Account No. 05-7962-9 at the Albuquerque National Bank, Albuquerque, New Mexico. This method of financing replaces the voucher system described in paragraph 3.

5. There is an agreement among the corporation, the bank and the Department of Health, Education and Welfare concerning these funds, which is attached hereto as Exhibit B. This agreement was entered into two years before we began receiving our funds by a letter of credit but instead were submitting monthly vouchers. It remains applicable to the new funding arrangement.

6. The corporation does not mingle these funds in the account with any other funds it receives. It writes checks directly on this account to pay its own staff and outside suppliers.

7. When the corporation anticipates that expenditures have to be made, such as payroll payments, I complete Treasury Form TUS-5401 and bring it to the Albuquerque National Bank which transmits the form to the Federal Reserve Bank in Denver which credits the requested funds to our account. These funds are then available to cover the checks drawn on the account.

8. The corporation pays and will continue to pay New Mexico gross receipts tax on its payments from the Department of Health, Education and Welfare. These tax payments are allowable costs reimbursed by the federal agency.

/s/ Ernest Cuaron
ERNEST CUARON

Subscribed and sworn to before me on this 6th day of August, 1977.

/s/ [Illegible]
Notary Public

My Commission Expires: August 9, 1980

MAY 1973
6 TREASURY FRM 2000

ISSUING AGENCY	LETTER OF CREDIT	LETTER OF CREDIT NUMBER
NIH, DHS, NIH Bethesda, Md. 20014	Austin TREASURY DEPARTMENT CIRCULAR No. 1075, Revised	75-08-N706 AMENDMENT NUMBER 0
AGENCY STATION SYMBOL	(FOR AGENCY USE)	EFFECTIVE DATE
75-08-9701		AUGUST 1, 1977

TO: The Federal Reserve Bank	BRANCH BANK AT
DENVER	KANSAS CITY

In accordance with the authorization of the Fiscal Assistant Secretary, Treasury Department, there is hereby authorized for the account and responsibility of the issuing agency a letter of credit:

IN FAVOR OF	FOR DEPOSIT ONLY TO
New Mexico Professional Standards Review Organization 2650 Yale Blvd. S.E. Albuquerque, New Mexico 87106	Albuquerque National Bank 303 Roma NW Albuquerque, NM Acct # 05-7962-9 ACCOUNT

AMOUNT AUTHORIZED		PRIOR AUTHORIZATION	THIS CHANGE
$ 58,000.00	☒ EACH MONTH ☐ EACH QUARTER ☐ WITHOUT TIME LIMIT ☐ _____	$ -0.00-	Increase $ Decrease $

☐ The unpaid balance of this letter of credit will remain available until you are advised in writing by the Treasury Department that this letter has been revoked.*

OR

☐ The unpaid balance of this letter of credit is revoked at the end of each period indicated and the full amount reestablished at the beginning of the following period until you are advised in writing by the Treasury Department that this letter has been revoked.*

The amount of this letter of credit is hereby certified to be drawn against, upon presentation to you of Form TUS 5401, Payment Voucher on Letter of Credit, by the official(s) of the recipient organization whose signature(s) appear(s) on the Standard Form 1194, Authorized Signature Card for Payment Vouchers on Letter of Credit, attached hereto or previously or subsequently furnished you through the Treasury Department.

The amount of each payment voucher paid by a Federal Reserve Bank or branch to a designated commercial bank for credit to the account of the recipient organization shall constitute payment to the recipient organization by the United States.

I certify to the Treasury Department that the payments authorized herein are correct and proper for payment from the appropriations or funds legally committed and available for the purpose, when paid in accordance with the terms and condition cited above.

*This letter of credit is irrevocable to the extent the recipient organization has obligated funds in good faith thereunder in executing the authorized Federal program in accordance with the grant, contract, or other agreement.

NEW LETTER OF CREDIT

JULY 22, 1977 — ARTHUR L. FRANISKI, JR.

DATE CERTIFIED — AUTHORIZED CERTIFYING OFFICER

CHIEF, DEPOSITARY LIAISON SECT.

TYPED NAME AND TITLE

1193-103

EXHIBIT B

AGREEMENT FOR SPECIAL BANK ACCOUNT

Agreement entered into this 18th day of July, 1975 between the United States of America, hereinafter called the Government, represented by the Contracting Officer executing this Agreement, New Mexico Professional Standards Review Organization, a corporation under the laws of New Mexico hereinafter called the Contractor, and the Albuqueque National Bank, a banking corporation under the laws of the State of New Mexico located at 123 Central NW hereinafter called the Bank.

RECITALS

(a) Under the date of November 4, 1974 the Government and the Contractor entered into Contract No. HSA 105-240-75-0003 providing for the making of advance payments to the Contractor. Copy of such advance payment provisions has been furnished to the Bank.

(b) Said Contract requires that amounts advanced to the Contractor thereunder be deposited in a Special Bank Account or accounts at a member bank or banks of the Federal Reserve System or any "insured" bank within the meaning of the Act creating the Federal Deposit Insurance Corporation (Act of August 23, 1935; 49 Stat. 684, as amended; 12 U.S.C. 264), separate from the Contractor's general or other funds; and, the Bank being such a bank, the parties are agreeable to so depositing said amounts with the Bank.

(c) This Special Bank Account shall be designated The New Mexico Professional Standards Review Organization Health Services Administration Special Bank Account.

COVENANTS

In consideration of the foregoing, and for other good and valuable considerations, it is agreed that;

(1) The Government shall have a lien upon the credit balance in said account to secure the repayment of all advance payments made to the Contractor, which lien shall be superior to any lien or claim of the bank with respect to such account.

(2) The Bank will be bound by the provisions of said contract or contracts relating to the deposit and withdrawal of funds in the above Special Bank Account, but shall not be responsible for the application of funds withdrawn from said account. After receipt by the Bank of written directions from the Contracting Officer, or from the Administering Office designated in the advance payment contract mentioned above, or from the duly authorized representative of the Contracting Officer or the Administering Office, the Bank shall act thereon and shall be under no liability to any party hereto for any action in accordance with the said written directions. Any written directions received by the Bank through the Contracting Officer upon Health Services Administration stationery and purporting to be signed by, or by the direction of the Contracting Officer or his duly authorized representative, shall insofar as the rights, duties, and liabilities of the Bank are concerned, be conclusively deemed to have been properly issued and filed with the Bank by the Health Services Administration.

(3) The Government, or its authorized representatives, shall have access to the books and records maintained by the Bank with respect to such Special Bank account at all reasonable times and for all reasonable purposes, including (but without limiting and generality thereof) the inspection or copying of such

books and records and any and all memoranda, checks, correspondence or documents appertaining thereto. Such books and records shall be preserved by the Bank for a period of six (6) years after the closing of this Special Bank Account.

(4) In the event of the service of any writ of attachment, levy of execution, or commencement of garnishment proceedings with respect to the Special Bank Account, the Bank will promptly notify the Accounting and Finance Section, Health Services Administration, Rockville, Maryland 20852.

IN WITNESS THEREOF the parties hereto have caused this agreement to be executed as of the day and year first above written.

CONTRACTOR

By /s/ [Illegible]
Contractor's Representative

/s/ Secretary
Title

By /s/ [Illegible]
Bank's Representative

Assistant Cashier
Title

UNITED STATES OF AMERICA

By /s/ Albert E. [illegible]
Government's Representative

Contracting Officer
Title

EDC/gm/7.25

ZIA COMPANY STANDARD TERMS AND CONDITIONS FOR FIXED PRICE PURCHASE ORDERS (Rev 6-75)

(EXHIBIT 1 TO WENDELL L. MILLER AFFIDAVIT) (R. II)

1. DEFINITIONS: As used throughout this order, the following terms shall have the meaning set forth below:

   (a) The term "Government" means the United States of America.

   (b) The term "ERDA" means the United States Energy Research & Development Administration or any duly authorized representative thereof, including the Contracting Officer except for the purpose of deciding an appeal under the article entitled "Disputes."

   (c) The term "Contracting Officer" means the person executing the prime contract on behalf of the Government and includes his successors or any duly authorized representative of any such person.

   (d) The term "Buyer" means THE ZIA COMPANY in the performance of the prime contract W-17-028-ENG-90 with the United States of America and includes any duly authorized representative thereof.

   (e) Except as otherwise provided in this order, the term "subcontracts" includes purchase orders under this purchase order.

2. CHANGES: The Buyer may at any time, by a written order, and without notice to the sureties, make changes, within the general scope of this order, in any one or more of the following: (i) Drawings, designs, or specifications, where the supplies to be furnished are to be specially manufactured for the Buyer in accordance therewith; (ii) method of shipment or packing; and (iii) place of delivery. If any

such change causes an increase or decrease in the cost of, or the time required for, the performance of any part of the work under this order, whether changed or not changed by any such order, an equitable adjustment shall be made in the order price or delivery schedule, or both, and the order shall be modified in writing accordingly. Any claim by the seller for adjustment under this article must be asserted within 30 days from the date of receipt by the Seller of the notification of change: Provided, however, That the Buyer, if he decides that the facts justify such action, may receive and act upon any such claim asserted at any time prior to final payment under this order, where the cost of property made obsolete or excess as a result of a change is included in the Seller's claim for adjustment, the Buyer shall have the right to prescribe the manner of disposition of such property. Failure to agree to any adjustment shall be a dispute concerning a question of fact within the meaning of the article of this order entitled "Disputes." However, nothing in this article shall excuse the Seller from proceeding with the order as changed.

3. EXTRAS: Except as otherwise provided in this order, no payment for extras shall be made unless such extras and the price therefor have been authorized in writing by the Buyer.

3. VARIATION IN QUANTITY: No variation in the quantity of any item called for by this order will be accepted unless such variation has been caused by conditions of loading, shipping, or packing, or allowances in manufacturing processes, and then only to the extent, if any, specified elsewhere in this order.

5. INSPECTION:

(a) All supplies (which term throughout this article includes without limitation raw materials, com-

ponents, intermediate assemblies, and end products) shall be subject to inspection and test by the Buyer and ERDA, to the extent practicable at all times and places including the period of manufacture, and in any event prior to acceptance.

(b) In case any supplies or lots of supplies are defective in material or workmanship or otherwise not in conformity with the requirements of this order, the Buyer shall have the right either to reject them (with or without instructions as to their disposition) or to require their correction. Supplies or lots of supplies which have been rejected or required to be corrected shall be removed or, if permitted or required by the Buyer, corrected in place by and at the expense of the Seller promptly after notice, and shall not thereafter be tendered for acceptance unless the former rejection or requirement of correction is disclosed. If the Seller fails promptly to remove such supplies or lots of supplies which are required to be removed, or promptly to replace or correct such supplies or lots of supplies, the Buyer either (i) may by subcontract or otherwise replace or correct such supplies and charge to the Seller the cost occasioned the Buyer thereby, or (ii) may terminate this order for default as provided in the article of this order entitled "Default." Unless the Seller corrects or replaces such supplies within the delivery schedule, the Buyer may require the delivery of such supplies at a reduction in price which is equitable under the circumstances. Failure to agree to such reduction of price shall be a dispute concerning a question of fact within the meaning of the article of this order entitled "Disputes."

(c) If any inspection or test is made by the Buyer or the ERDA on the premises of the Seller or a subcontractor, the Seller without additional charge shall provide all reasonable facilities and assistance for the safety and convenience of the inspection by the Buyer or ERDA in the performance of their duties. If inspection by the Buyer or ERDA or test is made at a point other than the premises of the Seller or a subcontractor, it shall be at the expense of the Buyer except as otherwise provided in this order; Provided, That in case of rejection the Buyer shall not be liable for any reduction in value of samples used in connection with such inspection or test. All inspections and tests by the Buyer or ERDA shall be performed in such a manner as not to unduly delay the work. The Buyer reserves the right to charge to the Seller any additional cost of Buyer inspection and test when supplies are not ready at the time such inspection and test is requested by the Seller or when reinspection or retest is necessitated by prior rejection. Acceptance or rejection of the supplies shall be made as promptly as practicable after delivery, except as otherwise provided in this order; but failure to inspect and accept or reject supplies shall neither relieve the Seller from responsibility for such supplies as are not in accordance with the order requirements nor impose liability on the Buyer therefor.

(d) The inspection and test by the Buyer or ERDA of any supplies or lots thereof does not relieve the Seller from any responsibility regarding defects or other failures to meet the order requirements which may be discovered prior to acceptance. Except as otherwise provided in this order, acceptance shall be conclusive except as regards

latent defects, fraud, or such gross mistakes as amount to fraud.

(e) The Seller shall provide and maintain in inspection system acceptable to the Buyer covering the supplies hereunder. Records of all inspection work by the Seller shall be kept complete and available to the Buyer and ERDA during performance of this order and for such longer period as may be specified elsewhere in this order.

6. RESPONSIBILITY FOR SUPPLIES: Except as otherwise provided in this order, (i) the Seller shall be responsible for the supplies covered by this order until they are delivered at the designated delivery point, regardless of the point of inspection; and (ii) the Seller shall bear all risks as to rejected supplies after notice of rejection, except that the Buyer shall be responsible for the loss, or destruction or damage to the supplies only if such loss, destruction or damage results from the gross negligence of officers, agents, or employees of the Buyer acting within the scope of their employment.

7. PAYMENTS: The Seller shall be paid, upon the submission of proper invoices or vouchers, the prices stipulated herein for supplies delivered and accepted (dates be shown on the invoices or vouchers) or services rendered and accepted less deductions, if any, as herein provided. Unless otherwise specified, payment will be made on partial deliveries accepted by the Buyer when the amount due on such deliveries so warrants; or, when requested by the Seller, payments for accepted partial deliveries shall be made whenever such payment would equal or exceed either $1,000 or 50 percent of the total amount of this order.

8. EXAMINATION OF RECORDS: The Seller agrees that the Comptroller General of the United States or any of his duly authorized representatives shall, until

the expiration of three years after final payment under this order, or of the time periods for the particular records specified in Part 1-20 of the Federal Procurement Regulations of CFR Part 1-20), whichever expires earlier, have access to and the right to examine any directly pertinent books, documents, papers and records of Seller involving the actions related to this order: Provided, however, that this Article shall not apply to this order if the price of this order does not exceed Two Thousand Five Hundred no/100 Dollars ($2,500.00) or is an order for public utility services at rates established for uniform application to the general public. The periods of access and examination described herein shall continue until any Disputes appeals, litigation, or Comptroller General exceptions have been disposed of.

9. DEFAULT:

(a) The Buyer may, subject to the provisions of paragraph (c) below, by written notice of default to the Seller, terminate the whole or any part of this order in any one of the following circumstances:

(i) If the Seller fails to make delivery of the supplies or to perform the services within the time specified herein or any extension thereof; or

(ii) If the Seller fails to perform any of the other provisions of this order or so fails to make progress as to endanger performance of this order in accordance with its terms, and in either of these two circumstances does not cure such failure within a period of 10 days (or such longer periods the Buyer may authorize in writing) after receipt of notice from the Buyer specifying such failure.

(b) In the event the Buyer terminates this order in whole or in part as provided in paragraph (a) of this article, the Buyer may procure, upon such terms and in a manner as the Buyer may deem appropriate, supplies or services similar to those so terminated, and the Seller shall be liable to the Buyer for any excess costs for such similar supplies or services: Provided That the Seller shall continue the performance of this order to the extent not terminated under the provisions of this article.

(c) Except with respect to defaults of subcontractors, the Seller shall not be able for any excess costs if the failure to perform the order arises out of or beyond the control and without the fault or negligence of the Seller. Such causes may include, but are not restricted to, acts of God or of the public acts of the Government in either its sovereign or contractual capacity, fire, floods, epidemics, quarantine restrictions, strikes, freight embargoes, and unusually severe weather; but in every case the failure to perform must be beyond the control and without the fault or negligence of the Seller. If the failure to perform is caused by the default of a subcontractor, and if such default arises out of causes beyond the control of both the Seller and subcontractor and without the fault or negligence of either of them, the Seller shall not be liable for any excess costs for failure to perform, unless the supplies or services to be furnished by the subcontractor were obtainable from other sources in sufficient time to permit the Seller to meet the required delivery schedules.

(d) If this order is terminated as provided in paragraph (a) of this article the Buyer, in addition to any other rights provided in this article, may

require the Seller to transfer title to the Government and deliver to the Buyer or the Government in the manner and to the extent directed by the Buyer, (i) any completed supplies, and (ii) such partially completed supplies and material, parts, tools, dies, jigs, fixtures, plans, drawings, information, and purchase order rights (hereinafter called "manufacturing materials") as the Seller has specifically produced or specifically acquired for the performance of such of this order as has been terminated; and the Seller shall, upon direction from the Buyer, protect and preserve property in possession of the Seller in which the Buyer or the Government has an interest. Payment for completed supplies delivered to and accepted by the Buyer shall be at the order price. Payment for manufacturing materials delivered to and accepted by the Buyer and for the protection and preservation of property shall be in the amount agreed upon by Seller and Buyer; failure to agree to such amount shall be a dispute concerning a question of fact within the meaning of the article of this contract entitled "Disputes." The Buyer may withhold from amounts otherwise due the Seller for such completed supplies or manufacturing materials such sum as the Buyer determines to be necessary to protect the Buyer against loss because of outstanding liens or claims of former lien holders.

(e) If, after notice of termination of this order under the provisions of this article, it is determined for any reason that the Seller was not in default under the provisions of this article, or that the default was excusable under the provisions of this article, the rights and obligations of the parties shall be the same as if the notice of termination had been issued pursuant to the article

providing for termination for convenience of the Buyer.

(f) The rights and remedies of the Buyer and the Government provided in this article shall not be exclusive and are in addition to any other rights and remedies provided by law or under this order.

(g) As used in paragraph (c) of this clause, the terms "subcontractor" and "subcontractors" mean subcontractor(s) at any tier.

10. DISPUTES AND PAYMENT OF INTEREST ON SELLERS' CLAIM:

(a) Except as otherwise provided in this purchase order, any dispute concerning a question of fact arising under the order which is not disposed of by agreement shall be decided by the ERDA Contracting Officer for the prime contractor's Contract No. W-17-028-ENG-90, who shall reduce his decision to writing and mail or otherwise furnish a copy thereof to the price contractor and the Seller. The decision of the Contracting Officer shall be final and conclusive unless within 30 days from the date of receipt of such copy the Seller mails or otherwise furnishes to the Contracting Officer a written appeal addressed to ERDA. The decision of ERDA or its duly authorized representative for the determination of such appeals shall be final and conclusive unless determined by a court of competent jurisdiction to have been fraudulent, or capricious, or arbitrary, or so grossly erroneous. In connection with any appeal proceeding under this clause, the Seller shall be afforded an opportunity to be heard and to offer evidence in support of its appeal. Pending final decision of a dispute hereunder, the Seller shall proceed diligently

with the performance of this order and in accordance with Contracting Officer's decision.

(b) This disputes clause does not preclude consideration of law questions in connection with decisions provided for in paragraph (a) above; Provided, That nothing in this order shall be construed as making final the decision of any administrative official, representative, or board on question of law.

(c) If an appeal is filed by Seller from the final decision of the ERDA Contracting Officer for the Zia Company Contract W-17-028-ENG-90, under this Article denying a claim arising under this order, simple interest on the amount of the claim finally determined owed by the Zia Company shall be payable to the Seller in accordance with FPR 1-1.322.

11. BUY AMERICAN ACT:

(a) In acquiring end products, the Buy American Act (41 U.S. Code 10 a-d) provides that the Government give preference to domestic source end products. For the purpose of this article:

(i) "components" means those articles, materials, and supplies, which are directly incorporated in the end products;

(ii) "end products" means those articles, materials, and supplies, which are to be acquired under this order for public use; and

(iii) a "domestic source end product" means (A) an unmanufactured end product which has been mined or produced in the United States and (B) an end product manufactured in the United States if the cost of the components thereof which are mined, pro-

duced, or manufactured in the United States exceeds 50 per cent of the cost of all its components. For the purpose of this (a) (iii) (B), components of foreign origin of the same type or kind as the products referred to in (b) (ii) or (iii) of this article shall be treated as components mined, produced, or manufactured in the United States.

(b) The Seller agrees that there will be delivered under this order (by the Seller, Subcontractors, materialman, and suppliers) only domestic source end products, except end products:

(i) which are for use outside the United States;

(ii) which the Government determines are not mined, produced, or manufactured in the United States in sufficient and reasonable available commercial quantities and of a satisfactory quality;

(iii) as to which ERDA determines the domestic preference to be inconsistent with the public interest; or

(iv) as to which the Commission determines the cost to the Government to be unreasonable.

(The foregoing requirements are administered in accordance with Executive Order No. 10582, dated December 17, 1954.)

12. BILLS OF LADING WHERE DELIVERY IS AT POINT OF ORIGIN: The following clause shall be specified in all commercial bills of lading used by the Seller in making shipments hereunder where delivery is at point of origin: "This shipment is for the account of the U.S. Government which will assume

the freight charges, and is subject to the terms and conditions set forth in the standard form of the U.S. Government bill of lading and to any available special rates or charges."

13. CONTRACT WORK HOURS AND SAFETY STANDARDS ACT—OVERTIME COMPENSATION: This order, to the extent that it is of a character specified in the Contract Work Hours and Safety Standards Act (40 U.S.C. 327-333), is subject to the following provisions and to all other applicable provisions and exceptions of such Act and the regulations of the Secretary of Labor thereunder.

(a) OVERTIME REQUIREMENTS: No Seller or subcontractor contracting for any part of the Purchase Order work which may require or involve the employment of laborers, mechanics, apprentices, trainees, watchmen, and guards shall require or permit any laborer, mechanic, apprentice, trainee, watchman, or guard in any workweek in which he is employed on such work in excess of 8 hours in any calendar day or in excess of 40 hours in such workweek on work subject to the provisions of the Contract Work Hours and Safety Standards Act unless such laborer, mechanic, apprentice, trainee, watchman, or guard receives compensation at a rate not less than one and one-half times his basic rate of pay for all such hours worked in excess of 8 hours in any calendar day or in excess of 40 hours in such workweek, whichever is the greater number of overtime hours.

(b) VIOLATION; LIABILITY FOR UNPAID WAGES; LIQUIDATED DAMAGES: In the event of any violation of the provisions of paragraph (a), the Seller and any subcontractor responsible therefor shall be liable to any affected

employee for his unpaid wages. In addition, such Seller and subcontractor shall be liable to the United States for liquidated damages. Such liquidated damages shall be computed with respect to each individual laborer, mechanic, apprentice, trainee, watchman or guard employed in violation of the provisions of paragraph (a) in the sum of $10 for each calendar day on which such employee was required or permitted to be employed on such work in excess of 8 hours or in excess of his standard workweek of 40 hours without payment of the overtime wages required by paragraph (a).

(c) WITHHOLDING FOR UNPAID WAGES AND LIQUIDATED DAMAGES: The Buyer may withhold from the Seller, from any moneys payable on account of work performed by the Seller or subcontractor, such sums as may administratively be determined to be necessary to satisfy any liabilities of such Seller or subcontractor for unpaid wages and liquidated damages as provided in the provisions of paragraph (b).

(d) SUBCONTRACTS: The Seller shall insert paragraphs (a) through (d) of this clause in all subcontracts, and shall require their inclusion in all subcontracts of any tier.

(e) RECORDS: The Seller shall maintain payroll records containing the information specified in 29 CFR 516.2(a). Such records shall be preserved for 3 years from the completion of the contract.

14. WALSH-HEALEY PUBLIC CONTRACTS ACT: If this order is for the manufacture or furnishing of materials, supplies, articles, or equipment in an amount which exceeds or may exceed $10,000 and is otherwise subject to the Walsh-Healey Public Con-

tracts Act, as amended (41 U.S. Code 35-45), there are hereby incorporated by reference all representations and stipulations required by said Act and regulations issued thereunder by the Secretary of Labor, such representations and stipulations being subject to all applicable rulings and interpretations of the Secretary of Labor which are now or may hereafter be in effect.

15. EQUAL OPPORTUNITY: The following article is applicable unless this order is exempt under the rules and regulations and relevant orders of the Secretary of Labor (41 CFR. ch. 60).

During the performance of this order, the Seller agrees as follows:

(a) The Seller will not discriminate against any employee or applicant for employment because of race, color, religion, sex or national origin. The Seller will take affirmative action to ensure that applicants are employed, and that employees are treated during employment without regard to their race, color, religion, sex or national origin. Such action shall include, but not be limited to, the following: employment, upgrading, demotion or transfer; recruitment or recruitment advertising; layoff or termination; rates of pay or other forms of compensation; and selection for training, including apprenticeship. The Seller agrees to post in conspicuous places, available to employees and applicants for employment, notices to be provided by the Buyer setting forth the provisions of this Equal Opportunity article.

(b) The Seller will, in all solicitations or advertisements for employees placed by or on behalf of the Seller, state that all qualified applicants will receive consideration for employment without regard to race, color, religion, sex or national origin.

(c) The Seller will send to each labor union or representative of workers with which it has a collective bargaining agreement or other contract or understanding, "a notice to be provided by the Buyer, advising the labor union or workers' representative of the Seller's commitments under this "Equal Opportunity Clause," and shall post copies of the notice in conspicuous places available to employees and applicants for employment.

(d) The Seller will comply with all provisions of Executive Order No. 11246 of September 24, 1965 and of the rules, regulations, and relevant orders of the Secretary of Labor.

(e) The Seller will furnish all information and reports required by Executive Order No. 11245 of September 24, 1965 and by the rules, regulations and orders of the Secretary of Labor, or pursuant thereto, and will permit access to his books, records, and accounts by ERDA and the Secretary of Labor for purposes of investigation to ascertain compliance with such rules, regulations and orders.

(f) In the event of the Seller's noncompliance with the Equal Opportunity article of this order or with any of the said rules, regulations, or orders, this order may be cancelled, terminated, or suspended in whole or in part and the Seller may be declared ineligible for further Government orders in accordance with procedures authorized in Executive Order No. 11246 of September 24, 1965, and such other sanctions may be imposed and remedies invoked as provided in the said Executive Order or by rule, regulation, or order of the Secretary of Labor, or as otherwise provided by law.

(g) The Seller will include the provisions of paragraphs (a) through (g) in every subcontract or purchase order unless exempted by rules, regulations, or orders of the Secretary of Labor issued pursuant to Section 204 of Executive Order No. 11246 of September 24, 1965, so that such provisions will be binding upon each subcontractor or vendor. The Seller will take such action with respect to any subcontractor or purchase order as ERDA may direct as a means of enforcing such provisions, including actions for noncompliance: Provided, however, That in the event the Seller becomes involved in, or is threatened with, litigation with a subcontractor or vendor as a result of such direction by ERDA, the Seller may request the Government to enter into such litigation to protect the interests of the Government.

16. COMMERCIAL WARRANTY:

(a) The Seller agrees that the supplies or services furnished under this order shall be covered by the most favorable commercial warranties the Seller gives to any customer for the same or substantially similar supplies or services and that the rights and remedies provided by this article shall extend to the Government and are in addition to and do not limit any rights afforded to Buyer by any other article of this order.

(b) The Seller shall furnish to the Buyer copies of the most favorable commercial warranties the Seller gives to any customer for the same or substantially similar supplies or services, and such warranties shall be deemed a part of this purchase order.

17. CONVENANT AGAINST CONTINGENT FEES: Seller warrants that no persons or selling agency has

been employed or retained to solicit or secure this order upon an agreement or understanding for a commission, percentage, brokerage, or contingent fee, excepting bona fide employees or bona fide established commercial or selling agencies maintained by the Seller for the purpose of securing business. For breach or violation of this warranty the Buyer shall have the right to annul this order without liability or in its discretion to deduct from the purchase order price or consideration, or otherwise recover, the full amount of such commission, percentage, brokerage, or contingent fee.

18. UTILIZATION OF SMALL BUSINESS CONCERNS: (Applies if the value of this order exceeds $5,000.)

(a) It is the policy of the Government as declared by the Congress that a fair proportion of the purchases and contracts for supplies and services for the Government be placed with small business concerns.

(b) Seller agrees to accomplish the maximum amount of subcontracting to small business concerns that Seller finds to be consistent with the efficient performance of this order.

19. UTILIZATION OF LABOR SURPLUS AREA CONCERNS: (Applies if the value of this order exceeds $5,000.)

(a) It is the policy of the Government to award orders to labor surplus area concerns that (1) have been certified by the Secretary of Labor (hereafter referred to as certified-eligible concerns with first or second preferences) regarding the employment of a proportionate number of disadvantaged individuals and have agreed to perform substantially (i) in or near sections

of concentrated unemployment or underemployment or in persistent or substantial labor surplus areas or (ii) in other areas of the United States, respectively, or (2) are noncertified concerns which have agreed to perform substantially in persistent or substantial labor surplus areas, where this can be done consistent with the efficient performance of the order and at prices no higher than are obtainable elsewhere. The Seller agrees to use his best efforts to place his subcontracts in accordance with this policy.

(b) In complying with paragraph (a) of this Article and with paragraph (b) of the Article of this order entitled "Utilization of Small Business Concerns" the Seller in placing his subcontracts shall observe the following order of preference: (1) Certified-eligible concerns with a first preference which are also small business concerns; (2) other certified eligible concerns with a first preference; (3) certified-eligible concerns with a second preference which are also small business concerns; (4) other certified-eligible concerns with a second preference; (5) persistent or substantial labor surplus area concerns which are also small business concerns; (6) other persistent or substantial labor surplus area concerns; and (7) small business concerns which are not labor surplus area concerns.

20. DISCOUNTS: Discount time will be computed from whichever of the following dates is the latest: (1) the date of delivery of the supplies to carrier (when delivery is f.o.b. at point of origin), (2) the date of delivery at destination (when delivery is f.o.b. at point of destination), (3) the date correct invoice or voucher is received in the office specified by the buyer. Payment is deemed to be made, for the pur-

pose of earning the discount, on the date of mailing of the Buyer's check.

21. ASSIGNMENT. This order is assignable by Buyer to the Government or its designee. Neither this order nor any interest therein nor claim thereunder shall be assigned or transferred by the Seller except as expressly authorized in writing by the Buyer.

22. FEDERAL, STATE, AND LOCAL TAXES:

(a) Except as may be otherwise provided in this order, the price includes all applicable federal, state and local taxes and duties.

(b) Notwithstanding the provisions of (a) above, if the Seller intends to collect from the Buyer under this order any amount attributable to taxes imposed by the New Mexico Gross Receipts and Compensating Tax Act, such amount shall be separately stated in the price provision of this order and in Seller's invoices. The Seller warrants that, except as separately stated in the price provision in accordance with this paragraph (b), the price does not include any amounts attributable to taxes imposed by the New Mexico Gross Receipts and Compensating Tax Act or contingencies for such taxes.

(c) With respect to any taxes separately stated in the price provision of this order and on Seller's invoices in accordance with paragraph (b) the Buyer agrees either (1) to furnish to the Seller a non-taxable transaction certificate, or other document acceptable to the New Mexico Bureau of Revenue for purposes of precluding the application of such taxes to the Seller on account of this transaction or (2) to pay to the Seller any portion of such separately stated amount that

Seller is required to pay to the New Mexico Bureau of Revenue because of Buyer's inability to furnish such certificate or other document.

23. PROPERTY:

(a) Title to material purchases hereunder shall pass directly from the Seller to the Government at the point of delivery which shall be at Seller's plant—or such other point as may be specified in this order.

(b) (1) (Applicable if this order involves Government property furnished by Buyer to Seller herein called "Buyer-furnished property.") The delivery schedules set forth in this order are based upon the expectation that the Buyer-furnished property is not delivered to the Seller by such time, the Buyer shall, if requested by the Seller, determine if any delay has been occasioned the Seller thereby, and if so shall grant a reasonable extension of the time for completion of performance. The Buyer shall not be liable to Seller for damages of loss of profit by reason of any delay in delivery of said Buyer-Furnished property, except that in case of such delay, upon written request of the Seller, an equitable adjustment shall be made in the delivery schedule of this order, or price, or both, and in other contractual provisions affected thereby, in accordance with the procedures provided for in the article entitled "Changes."

(2) (Applicable if this order involves Seller-acquired property.) In connection with its work under this order, the Seller shall ac-

quire or manufacture for the Buyer's account property (such as special tooling or facilities) listed in the order hereinafter referred to as "Seller-acquired property."

(c) Title to all Buyer-furnished or Seller-acquired property shall remain in the Government. Title hereto shall not be affected by the incorporation or attachment thereof to any property not owned by the Government, nor shall any such property, or any part thereof, be or become a fixture or lose its identity as personalty by reason of affixation to any realty. The Seller shall maintain adequate property control records of such property consistent with good business practice and as may be prescribed by the Buyer; and small cause all such property to be to be clearly marked (if not so marked) to show that it is property of the Government.

(d) Buyer-furnished or Seller-acquired property shall be used only for the performance of this order.

(e) The Seller shall, in accordance with sound industrial practice and without additional cost to the Buyer, maintain in operating condition, repair, protect, and preserve such Buyer-furnished or Seller-acquired property until disposed of by the Seller in accordance with this article. Should any replacement of any such property become necessary during the term of this order other than by reason of the negligence or fault of the Seller, the same shall be made by the Seller at the direction of and for the account of the Buyer and the title thereto shall vest in the Government and any delay occasioned thereby shall be considered an excusable delay under this order.

(f) (1) Except for loss or destruction of, or damage to, Buyer-furnished or Seller-acquired property resulting from a failure of the Seller, due to wilful misconduct or lack of good faith of the Seller's managerial personnel to maintain in operating condition, repair, protect, and preserve such property as required by subparagraph (e) hereof, the Seller shall not be liable for loss or destruction of, or damage to, such property (i) caused by any peril while the property is in transit off the Seller's premises, or (ii) caused by any of the following perils while the property is on the Seller's premises, or on any other premises where such property may properly be located or by removal therefrom because of any of the following perils: Fire; lightning; windstorm; cyclone; tornado; hail; explosion; riot attending a strike; civil commotion; vandalism and malicious mischief; aircraft or objects falling therefrom; vehicles running on land or tracks (excluding vehicles owned or operated by the Seller or any agent or employee of the Seller); smoke; springler leakage; earthquake or volcanic eruption; flood, meaning thereby raising of rivers or streams; enemy attack or any action by the military, navy, or air forces of the United States in resisting enemy attack.

The perils as set forth above are hereinafter called "excepted perils." The term "Seller's managerial personnel," as used in this article, means the Seller's directors, officers, and such of its managers, superintendents, or other equivalent representatives who have supervision or direction of

(1) all of or substantially all of the Seller's business; or (2) all or substantially all of the Seller's operation at any one plant or separate location at which the work is being performed; or (3) a separate or complete major industrial operation in connection with performance of the order; or (4) a separate and complete major construction, alteration, or repair operation in connection with performance of the order.

(2) Upon the happening of loss or destruction of, or damage to, Buyer-furnished or Seller-acquired property, the Seller shall communicate with the Buyer and shall take all reasonable steps to protect such property, put all such property in the best possible order, and furnish to the Buyer a statement of (i) the loss, destroyed, and damaged Buyer-furnished or Seller-acquired property, (ii) the time and origin of the loss, destruction, or damage, (iii) all known interests in the commingled property of which such is a part, and (iv) the insurance, if any, covering any part of or interest in such commingled property.

(3) With the approval of the Buyer after loss or destruction of, or damage to, the Buyer-furnished or Seller-acquired property, and subject to such conditions and limitations as may be imposed by the Buyer, the Seller shall, in order to minimize the loss to Buyer and the Government or in order to permit resumption of business or the like, sell for the account of the Government, any item of such property which has been damaged beyond practicable repair, or which is so commingled or combined with property of

others, including the Seller, that separation is impracticable.

(4) Except to the extent of any loss or destruction, or damage to, Buyer-furnished or Seller-acquired property for which the Seller is relieved of liability under the foregoing provisions of this paragraph, and except for reasonable wear and tear or depreciation, or the utilization or disposition of such property in accordance with the provisions of this order the property shall be returned to the Buyer in as good condition as was received by the Seller.

(5) In the event the Seller is indemnified, reimbursed, or compensated for any loss or destruction of, or damage to Buyer-furnished or Seller-acquired property caused by an excepted peril, it shall equitably reimburse Buyer or the Government. The Seller shall do nothing to prejudice the Government's rights to recover against third parties for any such loss, destruction or damage and upon the request of the Buyer shall, at the Government's expense, furnish to the Government all reasonable assistance and cooperation (including the prosecution or suits, and to execution of instructions of assignment in favor of the Government) in obtaining recovery.

(g) The Buyer and the Government shall at all times have access to the premise wherein any Buyer-furnished or Seller-acquired property is located.

(h) Upon the completion of this order, the Seller shall submit, in a form acceptable to the Buyer,

inventory schedule covering all items of Buyer-furnished or Seller-acquired property not consumed in the performance of this order (including any resulting scrap) or not theretofore delivered to the Buyer, and shall hold the same at no charge to the Buyer for a period of sixty days, unless the period of time is extended by mutual agreement. At the expiration of such period or upon the Buyer's earlier order the Seller shall dismantle, prepare for shipment and shall store or deliver said property to the Buyer on cars, trucks at Seller's plant at the expense of the Buyer, or make such other disposal of said property as may be directed by the Buyer. The net proceeds for any such disposal shall be credited to the purchase order price or shall be paid over as the Buyer may direct.

24. TERMINATION FOR CONVENIENCE:

(a) The performance of work under this order may be terminated in whole, or from time to time in part, by the Buyer in accordance with this article. Any such termination shall be effected by delivery to the Seller of a Notice of Termination specifying the extent to which performance of work under the order is terminated, and the date upon which such termination becomes effective.

(b) After receipt of a Notice of Termination, and except as otherwise directed by Buyer, the Seller shall:

(1) Stop work under the order on the date and to the extent specified in the Notice of Termination;

(2) Place no further subcontracts for materials, services, or facilities, except as may be

necessary for completion of such portion of the work under the order as is not terminated;

(3) Terminate all subcontracts to the extent that they relate to the performance of work terminated by the Notice of Termination;

(4) Assign to the Buyer, in the manner, at the times, and to the extent —— by the Buyer, all of the rights, title and interests of the Seller under subcontracts so terminated, in which case the Buyer shall have the rule in its discretion, to settle or pay any or all claims arising out of the termination of such subcontracts;

(5) Settle all outstanding liabilities and all claims arising out of such termination of orders and subcontracts, with the approval or ratification of the Buyer, to the extent he may require, which approval or ratification shall be final for all the purposes of this article;

(6) Transfer title to the Government and deliver in the manner, at the time and to the extent, if any, directed by the Buyer (i) the fabrication of unfabricated parts, work in process, completed work, supplies, and of material produced as a part of, or acquired in connection with the performance of, the work terminated by the Notice of Termination, and (ii) the completed or partially completed plans, drawings, information and other property which, if the order had been completed, would have been required to be furnished to the Buyer;

(7) Use his best efforts to sell, in the manner, at the time, to the extent and at the price or prices directed or authorized by the Buyer, any property of the types referred to in (6) above: Provided, however, that the Seller (i) shall not be required to extend credit to any purchaser and (ii) may acquire any such property under the conditions prescribed by and at a price or prices approved by the Buyer; And provided further, That the proceeds of any such transfer or disposition shall be applied to reduction of any payments to be made by the Buyer to the Seller under order or shall otherwise be credited to the price or cost of the work covered by this order or paid in such other manner as the Buyer may choose;

(8) Complete performance of such part of the work as shall not have been ——ted by the Notice of Termination; and

(9) Take such action, as may be necessary, or as the Buyer may direct, for protection and preservation of the property related to this order within the possession of the Seller and in which the Buyer or the Government has or may acquire an interest.

At any time after expiration of the plant clearance period, as defined in part 1-8.1 of the Federal Procurement Regulations (41 CFR 1-8.1), as the ——tion may be amended from time to time, the Seller may submit to the Buyer certified as to quantity and quality, or any or all items of termination ——tory not previously disposed of, exclusive of items the disposition of which has been directed or authorized by the Buyer, and may request the Buyer to

move such items or enter into a storage agreement covering them. Not later than fifteen (15) days thereafter, the Government will accept title to such items remove them or enter into a storage agreement covering the same: Provided the list submitted shall be subject to verification by the Buyer upon re——— the items or, if the items are stored, within forty-five (45) days from time of submission of the list, and any necessary adjustment to correct the list submitted shall be made prior to final settlement.

(c) After receipt of a Notice of Termination, the Seller shall submit to the Buyer his termination claim, in the form and with certification prescribed by the Buyer. Such claim shall be submitted promptly but in no event later than —— year from the effective date of termination, unless one or more extensions in writing are granted by the Buyer upon request of the Seller made in writing within such one-year period or authorized extension thereof. However, if Buyer determines that the facts justify such action, he may receive and act upon any such termination claim at any time after such one-year period or extension thereof. Upon failure of the Seller to submit his termination —— within the time allowed, the Buyer may, subject to any review required by ERDA procedures in effect as of the date of execution of this order, determine, on the basis of information available to him, the amount, if any, due to the Seller by reason of the termination and shall thereupon pay to Seller the amount so determined.

SANDIA CORPORATION STANDARD TERMS AND CONDITIONS (EXHIBIT 1 TO CHARLES T. ROSS, JR. AFFIDAVIT (R. II)

A. The following Articles apply to this Contract unless specifically deleted, or except to the extent they are specifically supplemented or amended, in Section I.

ARTICLE A1—DEFINITIONS

As used throughout this contract, the following terms shall have the meanings set forth below:

(a) SANDIA—Sandia Corporation and Sandia Laboratories, operated by Sandia Corporation (both Sandia), a prime contractor to the United States Energy Research and Development Administration under Contract No. E(29-1)-789, as amended.

(b) GOVERNMENT—The United States of America.

(c) ERDA—The United States Energy Research and Development Administration (ERDA), the Administrator of Energy Research and Development, or any duly authorized representative of the Administrator including the Area Manager, Sandia Area Office, ERDA, except for the purpose of deciding an appeal under the article entitled "Disputes."

(d) CONTRACTOR—The Seller or the other party to the contract with Sandia.

(e) SUBCONTRACTS—Except as otherwise provided in this contract, the term "subcontracts" includes purchase orders under this contract.

ARTICLE A2—CHANGES

The Sandia Contracting Representative may at any time, by a written order, and without notice to the sureties, make changes, within the general scope of this contract, in any one or more of the following: (i) drawings, designs, or specifications, where the supplies to be furnished are to be specially manufactured for Sandia in accordance therewith; (ii) method of shipment or packing; and (iii) place of delivery. If any such change

causes an increase or decrease in the cost of, or the time required for, the performance of any part of the work under this contract, whether changed or not changed by any such order, an equitable adjustment shall be made in the contract price or delivery schedule, or both, and the contract shall be modified in writing accordingly. Any claim by the Contractor for adjustment under this Article must be asserted within 30 days from the date of receipt by the Contractor of the notification of change: Provided, however, That the Sandia Contracting Representative, if he decides that the facts justify such action, may receive and act upon any such claim asserted at any time prior to final payment under this contract. Where the cost of property made obsolete or excess as a result of a change is included in the Contractor's claim for adjustment, the Sandia Contracting Representative shall have the right to prescribe the manner of disposition of such property. Failure to agree to any adjustment shall be a dispute concerning a question of fact within the meaning of the Article of this contract entitled "Disputes." However, nothing in this Article shall excuse the Contractor from proceeding with the contract as changed.

ARTICLE A3—STOP WORK ORDER

(a) The Sandia Contracting Representative may, at any time, by written order to the Contractor, require the Contractor to stop all, or any part, of the work called for by this contract for a period of ninety (90) days after the order is delivered to the Contractor, and for any further period to which the parties may agree. Any such order shall be specifically identified as a Stop Work Order issued pursuant to this Article. Upon receipt of such an order, the Contractor shall forthwith comply with its terms and take all reasonable steps to minimize the incurrence of costs allocable to the work covered by the order during the period of work stoppage. Within a period of ninety (90) days after a stop

work order is delivered to the Contractor or within any extension of that period to which the parties shall have agreed, the Sandia Contracting Representative shall either—(i) cancel the stop work order, or (ii) terminate the work covered by such order as provided in the Article of this contract entitled "Termination for Convenience."

(b) If a stop work order issued under this Article is cancelled or the period of the order or any extension thereof expires, the Contractor shall resume work. An equitable adjustment shall be made in the delivery schedule, the contract price, or a combination thereof, and in any other provisions of the contract that may be affected, and the contract shall be modified in writing accordingly, if—(i) the stop work order results in an increase in the time required for, or in the Contractor's cost properly allocable to, the performance of any part of this contract, and (ii) the Contractor asserts a claim for such adjustment within thirty (30) days after the end of the period of work stoppage; provided that, if the Sandia Contracting Representative decides the facts justify such action, he may receive and act upon any such claim asserted at any time prior to final payment under this contract. Failure to agree to any adjustment shall be a dispute concerning a question of fact within the meaning of the Article of this contract entitled "Disputes."

(c) If a stop work order is not cancelled and the work covered by such order is terminated as provided by the Article of this contract entitled "Termination for Convenience," the reasonable costs resulting from the stop work order shall be allowed in arriving at the termination settlement.

ARTICLE A6—PAYMENTS

(a) The Contractor shall be paid, upon the submission of proper invoices or vouchers, the prices stipulated herein for supplies delivered and accepted or services rendered and accepted, less deductions, if any, as herein provided.

(b) For the purpose of computing discounts and other terms of payment, time will be computed from the date of receipt by Sandia of Contractor's correct invoices or the date of delivery of the supplies or services, whichever is later. Payment is deemed to be made for the purpose of earning the discount on the date of mailing of Sandia's checks.

ARTICLE A10—PROPERTY

(a) Title to material purchased hereunder shall pass directly from the Contractor to the Government at the designated delivery point.

(b) (1) (Applicable if this contract involves Government property furnished by Sandia to the Contractor herein referred to as "Sandia-furnished property.") The delivery schedules set forth in this contract are based upon the expectation that the Sandia-furnished property referred to in Section I of this contract will be delivered on or before the date or dates set forth in Section I. In the event that such Sandia-furnished property is not delivered to the Contractor by such time or times, the Sandia Contracting Representative shall, if requested by the Contractor, determine if any delay has been occasioned the Contractor thereby, and if so shall grant a reasonable extension of the time for completion of performance. Sandia shall not be liable to the Contractor for damages or loss of profit by reason of any delay in delivery of said Sandia-furnished property, except that in case of such delay, upon written request of the Contractor, an equitable adjustment shall be made in the delivery schedule of this contract, or price, or both, and in other contractual provisions affected thereby, in accordance with the procedures provided for in the Article entitled "Changes."

(2) (Applicable if this contract involves Contractor-acquired property.) In connection with its work under this contract, the Contractor shall, within the time or times specified in Section I, if any, acquire or manufac-

ture for the Government's account the property, such as special tooling, test equipment, and facilities, listed in Section I (herein referred to as "Contractor-acquired property.")

(c) Title to all Sandia-furnished or Contractor-acquired property shall remain in the Government. Title thereto shall not be affected by the incorporation or attachment thereof to any property not owned by the Government, nor shall any such property, or any part thereof, be or become a fixture or lose its identity as personality by reason of affixation to any realty. The Contractor shall maintain adequate property control records of such property consistent with good business practice and as may be prescribed by the Sandia Contracting Representative, and shall cause all such property to be clearly marked (if not so marked) to show that it is property of the Government.

(d) Unless otherwise authorized by the Sandia Contracting Representative, Sandia-furnished or Contractor-acquired property shall be used only for the performance of this contract.

(e) The Contractor shall, in accordance with sound industrial practice and without additional cost to Sandia or the Government, maintain in operating condition, repair, protect, and preserve such Sandia-furnished or Contractor-acquired property until disposed of by the Contractor in accordance with this Article. Should any replacement or repair of any such property become necessary during the term of this contract, for which the Contractor is not responsible under the provisions of this contract, the same shall be made by the Contractor at the direction of and for the account of Sandia, and the title thereto shall vest in the Government and any delay occasioned thereby shall be considered an excusable delay under this contract. Any replacement or repair of any such property for which the Contractor is responsible under the provisions of this contract shall be accomplished by the Contractor at his own expense.

* * * * *

(b) Violation; liability for unpaid wages; liquidated damages. In the event of any violation of the provisions of paragraph (a), the Contractor and any Subcontractor responsible therefor shall be liable to any affected employee for his unpaid wages. In addition, such Contractor and Subcontractor shall be liable to the United States for liquidated damages. Such liquidated damages shall be computed with respect to each individual laborer, mechanic, apprentice, trainee, watchman, or guard employed in violation of the provisions of paragraph (a) in the sum of $10 for each calendar day on which such employee was required or permitted to be employed on such work in excess of 8 hours or in excess of his standard workweek of 40 hours without payment of the overtime wages required by paragraph (a).

(c) Withholding for unpaid wages and liquidated damages. Sandia may withhold from the Contractor, any moneys payable on account of work performed by the Contractor or Subcontractor, such sums as Sandia determines to be necessary to satisfy any liabilities of such contractor or subcontractor for unpaid wages and liquidated damages as provided in the provisions of paragraph (b).

(d) Subcontracts. The Contractor shall insert paragraphs (a) through (d) of this Article in all subcontracts, and shall require their inclusion in all subcontracts of any tier.

(e) Records. The Contractor shall maintain payroll records containing the information specified in 29 CFR 516.2(A). Such records shall be preserved for 3 years from the completion of the contract.

ARTICLE A105—WALSH-HEALEY PUBLIC CONTRACTS ACT

If this contract is for the manufacture or furnishing of materials, supplies, articles, or equipment in an amount which exceeds or may exceed $10,000 and is otherwise subject to the Walsh-Healey Public Contracts

Act, as amended (41 U.S. Code 35-45), there are hereby incorporated by reference all representations and stipulations required by said Act and regulations issued thereunder by the Secretary of Labor, such representations and stipulations being subject to all applicable rulings and interpretations of the Secretary of Labor which are now or may hereafter be in effect.

ARTICLE A106—CONVICT LABOR

In connection with the performance of work under this contract, the Contractor agrees not to employ any person undergoing sentence of imprisonment except as provided by Public Law 89-176, September 10, 1965 (18 U.S.C. 4082(c)(2)) and Executive Order 11755, December 29, 1973.

ARTICLE A107—NOTICE OF LABOR DISPUTES

Whenever an actual or potential labor dispute is delaying or threatens to delay the performance of the work, the Contractor shall immediately notify the Sandia Contracting Representative in writing. Such notice shall include all relevant information concerning the dispute and its background.

ARTICLE A108—BUY AMERICAN ACT

(a) In acquiring end products, the Buy American Act (41 U.S. Code 10a-d) provides that the Government give preference to domestic source end products. For the purpose of this Article: (i) "Components" means those articles, materials, and supplies, which are directly incorporated in the end products; (ii) "End products" means those articles, materials and supplies, which are to be acquired under this contract for public use; and (iii) a "domestic source end product" means (A) an unmanufactured end product which has been mined or produced in the United States and (B) an end product manufactured in the United States if the cost of the

components thereof which are mined, produced, or manufactured in the United States exceed 50 percent of the cost of all its components. For the purposes of this (a) (iii) (B), components of foreign origin of the same type or kind as the products referred to in (b) (ii) or (iii) of this Article shall be treated as components mined, produced, or manufactured in the United States.

(b) The Contractor agrees that there will be delivered under this contract only domestic source end products, except end products: (i) which are for use outside the United States; (ii) which the Government determines are not mined, produced, or manufactured in the United States in sufficient and reasonably available commercial quantities and of a satisfactory quality; (iii) as to which ERDA determines the domestic preference to be inconsistent with the public interest; or (iv) as to which ERDA determines the cost to the Government to be unreasonable. (The foregoing requirements are administered in accordance with Executive Order No. 10582, dated December 17, 1954.)

ARTICLE A109—RENEGOTIATION

(a) This contract is subject to the Renegotiation Act of 1951 (50 U.S.C. App. 1211, et seq.), as amended, and to any subsequent act of Congress providing for the renegotiation of contracts. Nothing contained in this Article shall impose any renegotiation obligation with respect to this contract or any subcontract hereunder which is not imposed by an act of Congress heretofore or hereafter enacted. Subject to the foregoing this contract shall be deemed to contain all the provisions required by section 104 of the Renegotiation Act of 1951, and by any such other act, without subsequent contract amendment specifically incorporating such provisions.

(b) The Contractor agrees to insert the provisions of this Article, including this paragraph (b), in all subcontracts, as that term is defined in section 103g of the Renegotiation Act of 1951, as amended.

ARTICLE A110—UTILIZATION OF SMALL BUSINESS CONCERNS

(Applies if the amount of this contract exceeds $5,000.)

(a) It is the policy of the Government as declared by the Congress that a fair proportion of the purchases and contracts for supplies and services for the Government be placed with small business concerns.

(b) The Contractor agrees to accomplish the maximum amount of subcontracting to small business concerns that the Contractor finds to be consistent with the efficient performance of this contract.

ARTICLE A111—UTILIZATION OF LABOR SURPLUS AREA CONCERNS

(Applies if the amount of this contract exceeds $5,000.)

(a) It is the policy of the Government to award contracts to labor surplus area concerns that (1) have been certified by the Secretary of Labor (hereafter referred to as certified-eligible concerns with first or second preferences) regarding the employment of a proportionate number of disadvantaged individuals and have agreed to perform substantially (i) in or near sections of concentrated unemployment or underemployment or in persistent or substantial labor surplus areas or (ii) in other areas of the United States, respectively, or (2) are noncertified concerns which have agreed to perform substantially in persistent or substantial labor surplus areas, where this can be done consistent with the efficient performance of the contract and at prices no higher than are obtainable elsewhere. The Contractor agrees to use its best efforts to place its subcontracts in accordance with this policy.

(b) In complying with paragraph (a) of this Article and with paragraph (b) of the Article of this contract entitled "Utilization of Small Business Concerns" the Contractor in placing its subcontracts shall observe the

following order of preference: (1) Certified-eligible concerns with a first preference which are also small business concerns; (2) Other certified-eligible concerns with a first preference; (3) Certified-eligible concerns with a second preference which are also small business concerns; (4) Other certified-eligible concerns with a second preference; (5) Persistent or substantial labor surplus area concerns which are also small business concerns; (6) Other persistent or substantial labor surplus area concerns; and (7) Small business concerns which are not labor surplus area concerns.

ARTICLE A112—DISPUTES

(a) Except as otherwise provided in this contract, any dispute concerning a question of fact arising under this contract which is not disposed of by agreement of the parties hereto shall be decided by the Area Manager, Sandia Area Office, ERDA, who shall reduce his decision to writing and mail or otherwise furnish a copy thereof to Sandia and the Contractor. The decision of the Area Manager shall be final and conclusive unless, within 30 days from the date of receipt of such copy, the Contractor mails or otherwise furnishes to the Area Manager a written appeal addressed to ERDA. The decision of ERDA or its duly authorized representative for the determination of such appeals shall be final and conclusive unless determined by a court of competent jurisdiction to have been fraudulent, or capricious, or arbitrary, or so grossly erroneous as necessarily to imply bad faith, or not supported by substantial evidence. In connection with any appeal proceeding under this Article, the Contractor shall be afforded an opportunity to be heard and to offer evidence in support of its appeal. Pending final decision of a dispute hereunder, the Contractor shall proceed diligently with the performance of the contract and in accordance with the said Area Manager's decision.

(b) This "Disputes" article does not preclude consideration of law questions in connection with decisions

provided for in paragraph (a) above: Provided, That nothing in this contract shall be construed as making final the decision of any administrative official, representative, or board on a question of law.

ARTICLE A113—COVENANT AGAINST CONTINGENT FEES

The Contractor warrants that no person or selling agency has been employed or retained to solicit or secure this contract upon an agreement or understanding for a commission, percentage, brokerage, or contingent fee, excepting bona fide employees or bona fide established commercial or selling agencies maintained by the Contractor for the purpose of securing business. For breach or violation of this warranty the Government shall have the right to annul this contract without liability or in its discretion to deduct from the contract price or consideration, or otherwise recover, the full amount of such commission, percentage, brokerage, or contingent fee.

ARTICLE A114—OFFICIALS NOT TO BENEFIT

No member of or delegate to Congress, or resident commissioner, shall be admitted to any share or part of this contract, or to any benefit that may arise therefrom; but this provision shall not be construed to extend to this contract if made with a corporation for its general benefit.

ARTICLE A115—EQUAL OPPORTUNITY

The following clause is applicable unless this contract is exempt under the rules, regulations, and relevant orders of the Secretary of Labor (41 CFR, Ch. 60).)

During the performance of this contract, the Contractor agrees as follows:

(a) The Contractor will not discriminate against any employee or applicant for employment because of race, color, religion, sex, or national origin. The Contractor

will take affirmative action to ensure that applicants are employed, and that employees are treated during employment, without regard to their race, color, religion, sex, or national origin. Such action shall include, but not be limited to, the following: employment, upgrading, demotion or transfer; recruitment or recruitment advertising; layoff or termination; rates of pay or other forms of compensation; and selection for training, including apprenticeship. The Contractor agrees to post in conspicuous places, available to employees and applicants for employment, notices to be provided by the Sandia Contracting Representative setting forth the provisions of this Equal Opportunity Article.

(b) The Contractor will, in all solicitations or advertisements for employees placed by or on behalf of the Contractor, state that all qualified applicants will receive consideration for employment without regard to race, color, religion, sex, or national origin.

(c) The Contractor will send to each labor union or representative of workers with which it has a collective bargaining agreement or other contract or understanding, a notice, to be provided by the Sandia Contracting Representative, advising the labor union or workers' representative of the Contractor's commitments under this Equal Opportunity Article, and shall post copies of the notice in conspicuous places available to employees and applicants for employment.

(d) The Contractor will comply with all provisions of Executive Order No. 11246 of September 24, 1965, and of the rules, regulations, and relevant orders of the Secretary of Labor.

(e) The Contractor will furnish all information and reports required by Executive Order No. 11246 of September 24, 1965 and by the rules, regulations, and orders of the Secretary of Labor, or pursuant thereto, and will permit access to its books, records, and accounts by ERDA and the Secretary of Labor for purposes of investigation to ascertain compliance with such rules, regulations, and orders.

(f) In the event of the Contractor's noncompliance with the Equal Opportunity Article of this contract or with any of the said rules, regulations, or orders, this contract may be cancelled, terminated, or suspended in whole or in part, and the Contractor may be declared ineligible for further Government contracts in accordance with procedures authorized in Executive Order No. 11246 of September 24, 1965, and such other sanctions may be imposed and remedies invoked as provided in Executive Order No. 11246 of September 24, 1965, or by rule, regulation, or order of the Secretary of Labor, or as otherwise provided by law.

(g) The Contractor will include the provisions of paragraphs (a) through (g) in every subcontract or purchase order unless exempted by rules, regulations, or orders of the Secretary of Labor issued pursuant to Section 204 of Executive Order No. 11246 of September 24, 1965, so that such provisions will be binding upon each Subcontractor or vendor. The Contractor will take such action with respect to any subcontract or purchase order as ERDA may direct as a means of enforcing such provisions, including sanctions for noncompliance: Provided, however, That in the event the Contractor becomes involved in, or is threatened with, litigation with a Subcontractor or vendor as a result of such direction by ERDA, the Contractor may request the Government to enter into such litigation to protect the interests of the Government.

NOTE: Pursuant to paragraph (e) above, the Contractor shall file, and shall cause its subcontractors to file, complete and accurate reports required by the rules, regulations, and orders of the Secretary of Labor.

ARTICLE A116—ASSIGNMENT

This contract is assignable by Sandia to the Government or its designee. Any assignment by the Contractor of the work to be performed, in whole or in part, or of

any other interest hereunder without Sandia's written consent, except an assignment confined solely to moneys due or to become due, shall be void. It is expressly agreed that any such assignment of moneys shall be void to the extent that it attempts to impose upon Sandia obligations to the assignee additional to the payment of such moneys, or to preclude Sandia from dealing solely and directly with the Contractor in all matters pertaining hereto, including the negotiation of amendments or settlements of amounts due.

ARTICLE A117—RELEASES VOID

Sandia's and the Government's representatives shall not be required to waive or release any personal rights in connection with any visits to Contractor's or Subcontractor's premises and Contractor and Subcontractor agree that no such waiver or release shall be pleaded by Contractor or Subcontractor or by third persons in any action or proceeding.

ARTICLE A118—UNCLASSIFIED CONTRACT

(The provisions of this Article are not applicable if Article B1, SECURITY, is included in this contract.)

This contract is not classified; therefore, there is no expressed or implied approval for origination, transmission, or receipt of classified documents under this contract.

ARTICLE A119—COST ACCOUNTING STANDARDS

(Applies if (1) this contract is negotiated (as defined in paragraph (e) below), and (2) the amount of the contract exceeds $100,000, except where the price negotiated is based on (i) established catalog or market prices of commercial items sold in substantial quantities to the general public, or (ii) prices set by law or regulation, and except where the contract is exempt from the requirement by reason of Sec. 331.30(b) of Title 4, Code of Federal Regulations.

(a) Unless the Cost Accounting Standards Board has prescribed rules or regulations exempting the Contractor or this contract from standards, rules, and regulations promulgated pursuant to 50 U.S.C. App. 2168 (P. L. 91-379, August 15, 1970), or other statutory authority, the Contractor, in connection with this contract shall:

(1) By submission of a Disclosure Statement, disclose in writing his cost accounting practices as required by regulations of the Cost Accounting Standards Board. The required disclosures must be made prior to contract award unless the Sandia Contracting Representative provides a written notice to the Contractor authorizing post-award submission in accordance with regulations of the Cost Accounting Standards Board. The practices disclosed for this contract shall be the same as the practices currently disclosed and applied on all other contracts and subcontracts being performed by the Contractor and which contain this Cost Accounting Standards Article. If the Contractor has marked the Disclosure Statement to indicate that it contains trade secrets and commercial or financial information which is privileged and confidential, the Disclosure Statement shall be submitted directly to the U.S. Energy Research and Development Administration, Sandia Area Office, P.O. Box 5400, Albuquerque, N.M. 87115. The Disclosure Statement will be protected and will not be released outside of the Government.

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EXHIBIT 22AA TO PLAINTIFF'S SUPPLEMENTAL ANSWERS TO DEFENDANTS' INTERROGATORIES
(Second Set) 2/7/77 (R.V.)

March 19, 1954

Honorable W. Sterling Cole
Chairman, Joint Committee on
Atomic Energy
Congress of the United States

Dear Mr. Cole:

I refer to your letter of December 23, 1953 to Mr. Strauss, inquiring as to action taken by the Commission to procure certain items directly and furnish them to its contractors. I attach a report by the Office of the General Counsel on this question. That report describes in some detail the situations in which such direct procurement actions have been taken. You will note that in each case the Commission would contend, even if no change in its procurement practices had been made, that the transaction was tax exempt under provisions of the Federal Constitution or of state law applicable to all agencies of the Federal Government. Thus, the action taken has served merely to eliminate legal doubts that might otherwise have been thought to exist as to the tax exempt status of the transaction. You will note also that in Ohio, where such action has principally occurred, the State will receive substantial tax revenues from the construction of the Portsmouth plant.

As the previous report of the General Counsel, attached to Mr. Strauss' letter of December 22, 1953, indicated, the Commission has endeavored to act in accordance both with the legislation of Congress intended to place AEC on the same footing as other federal agencies with respect to state and local taxes and with the desire of the Administration that it keep expenses to a minimum. I am in accord with the view expressed by the Office of

the General Counsel that the actions described in the report constitute appropriate measures, consistent with the action of Congress, to avoid litigation and reduce expenses.

I regret that pressure of other legislative matters has delayed preparation of this reply.

Sincerely yours,

K. D. NICHOLS
General Manager

Enclosure:

Report by the Office of the
General Counsel

Distribution:
Addressee—Orig. & 1
Chairman—1
Gen. Mgr.—1
Cong. Comm.—2
OGC—3
OROO (Ould)—1

Mar 19 1954

REPORT: Clarification of Certain Statements Concerning AEC Policy on State and Local Taxation.

REFERENCE: Letter dated December 23, 1953, from W. Sterling Cole, Chairman of the Joint Committee on Atomic Energy, and letter dated December 22, 1953, from Lewis L. Strauss to W. Sterling Cole.

The Chairman of the Joint Commission on Atomic Energy has requested further clarification with respect to that part of the General Manager's instructions of October 1, 1953, which directs Managers of Operations to procure materials directly and furnish them to contractors where such direct procurement would result in substantial savings without adverse effect on contractor relationships or on the AEC program or schedules.

As was indicated in the report attached to the letter to Mr. Cole of December 22, 1953, the action of the Congress in repealing the last sentence of section 9(b) of the Atomic Energy Act of 1946 was intended "to place the Atomic Energy Commission on a basis identical to that of the rest of the Federal Government with respect to" state and local taxation. Senate Report No. 694, 83rd Cong., 1st Sess., p. 1. Consistently with that purpose this Commission has authorized and directed its contractors to claim tax exemption in situations in which such exemption would be claimed by contractors of other Government agencies. As that report also points out, in certain instances this Commission has, since October 1, 1953, procured materials directly for use of its contractors in order to achieve efficiencies and economies, including tax savings.

The direct procurement action is consistent with policies and procedures established long before October 1, 1953. AEC's cost-type contracts and its procurement procedures contemplate that the Government may, and

in some instances shall, furnish materials for the use of the contractor. Contracts of other Government agencies contain similar provisions. See, for example, Department of Defense, Armed Services Procurement Regulations, Sec. XIII. AEC has for a long time, for reasons of efficiency and economy, followed the policy that requirements for its contractors should be met from available government sources if procurement from those sources is economically advantageous to the Government. Pursuant to this policy, contractors have been furnished with materials from Government stores, and have been authorized to place delivery orders against Government supply contracts entered into between the General Services Administration and suppliers. In addition, beginning more than a year prior to October 1, 1953, in order to achieve efficiency and economy in procuring certain items for the three gaseous diffusion plants at Oak Ridge, Tenn., Portsmouth, Ohio, and —cah, Ky. the Oak Ridge Operations Office has engaged in a sizeable program of centralized direct procurement. Direct procurement has also been used in cases, for example, in which the articles to be procured were articles of which a division or affiliate of the AEC contractor was a producer.

The decisions of the Supreme Court in *Alabama* v. *King and Boozer*, 314 U.S. 1 and *Kern Limerick Co.* v. *Scurlock*, No. 115, decided February 3, 1954, clearly contemplate that the United States may, if it desires, procure directly materials which are to be used by its contractors in the performance of their contracts. In the *Kern-Limerick* case the Supreme Court had before it an arrangement which has been used by the Navy Department in cost-type contracts since 1942, under which the contractor undertook to procure all items needed for the performance of the contract as agent for the United States. The Court held that the Navy was authorized to procure these items directly and furnish them to its contractor; that it could do this procurement through an agent; and that under the procedures adopted by the

Navy Department the United States was the purchaser and the purchase was constitutionally exempt from state taxation. It reached this result notwithstanding the fact that payment was initially made out of the contractor's own funds, subject to later reimbursement.

While the foregoing, I believe, is sufficient to indicate the basis and authority for the provision of the General Manager's instructions to which Mr. Cole's letter refers, it may be helpful, in addition, to describe the scope and nature of the principal direct procurement actions taken by this Commission since October 1, 1953. They have involved (1) new arrangements for direct procurement of certain items for the Portsmouth, Ohio, plant and (2) certain changes in the procedure for procuring various items already being directly procured by this Commission under its centralized procurement plan at Oak Ridge or purchased against Government Supply Schedules.

(1). It is estimated that the State of Ohio will receive, during fiscal years 1954 and 1955, approximately 4.6 million dollars in sales and use taxes on procurements of property by lump sum contractors and subcontractors for use in or in connection with the construction of the Portsmouth plant, the cost of which will be indirectly borne by AEC through payment of increased contract prices. This procurement would have been considered tax exempt under section 9(b) of the Act as it stood prior to the recent amendment. AEC does not question the tax liability of such contractors.

On purchases by our cost-type contractors for the Portsmouth plant, however, steps are being taken to litigate, before the Ohio Board of Tax Appeals, the issue of liability for Ohio sales and use taxes. This Commission and its cost-type contractors, with the concurrence of the Department of Justice, are taking the position that on such procurement the United States is the real purchaser, so that the legal incidence of the tax is on the United States and the transaction is exempt within the

rule stated in *Alabama* v. *King and Boozer*, 314 U.S. 1, and recently reaffirmed by the United States Supreme Court in *Kern-Limerick Co.* v. *Scurlock*, No. 115, discussed above. This position is based on the following features of the contractual arrangement:

a. The purchase agreements with the vendor provided that the Government acquired title to the property directly from the vendor and that the contracts of purchase were for the benefit of and are assignable to the Government, and contained numerous other provisions for the benefit of and establishing rights in the Government.

b. It was expressly understood between AEC and the contractor that he would use Government Money, advanced to him for this purpose and held in a special account, to pay the vendors for these purchases and would not use his own private funds. (It is doubtful whether any contractor handling a job the size of Portsmouth—over a billion dollars—either could, or would, have financed the operation in any other way.)

Alternatively, the Commission and its contractors will contend that if the Board of Tax Appeals rejects the view that the United States purchases directly from the vendor, then it should hold that the contractor is purchasing for resale to the United States and the sale is exempt under state law as a sale for resale. Reliance is also placed on a rule of the Ohio Tax Department granting an exemption on certain procurements by construction contractors who work under so-called "breakdown" or "time and materials" contracts. The Ohio authorities have not been willing to recognize that our cost-type contractors are entitled to an exemption under either of these rules.

While the Commission believes its position as to this procurement by cost-type contractors is strongly supported by the recent decision in the *Kern-Limerick* case

and other precedents, it has felt it advisable also to minimize the area of dispute by taking action since October 1 to arrange for direct procurement of approximately $100,000,000 of materials which will be used in and become a part of the Commission's Portsmouth facilities. This has been done by having Peter Kiewit Sons' Co. (the AEC management contractor for construction) assign its purchase orders over $50,000 to the Commission, in accordance with provisions of the purchase orders expressly permitting such assignments. The tax officials of the State of Ohio have been advised of this action and have indicated their agreement that no tax is due on these assigned transactions. The estimated sales and use tax on the proceurement actions so assigned would have been about 3 million dollars; an additional 2 to 3 million dollars of tax is involved in the pending litigation on the remaining Kiewet purchase order.

It should be emphasized that in the case of those purchase orders which have been assigned, it is AEC's contention, even without an assignment of the purchase orders, that the transaction through its cost-type contractor involved a purchase by the United States, because of the fact that the purchase was made with Government funds and title passed direct to the United States. The passage of title to the Government under these purchase orders of its cost-type contractors is not merely passage of a "security" title, but operates to make the property Government property in all respects. Thereafter, the use, control, and disposition of such property are governed by the same criteria, rules, and procedures as are applicable to any Government property furnished to a contractor in connection with work performed for AEC and the property may be, and sometimes is, made available to other contractors or used at other sites. The materials so procured include electric motors, transformers, switch gear and other electrical equipment, structural steel, miscellaneous iron, pipe and

fittings, pumps, condensers, fans, air grills, and refrigerator equipment.

(2). The other area in which a change in procurement practices has been made since October 1, 1953, also concerns the Oak Ridge, Portsmouth and Paducah plants and involves purchased in which the Government was already named as the purchaser on the fact of the documents. As has already been mentioned, for more than a year prior to October 1, 1953, the Oak Ridge Operations Office had undertaken a sizeable central procurement program in connection with the gaseous diffusion plant expansion. Such procurement was made by direct contract between AEC and the vendor. For administrative purposes, arrangements were made for the prime construction contractors at the three sites, and the Oak Ridge plant operator, Carbide and Carbon Chemicals Company, to participate directly in the administration of the purchase contracts and to handle payment of the invoices. This centralized procurement was undertaken for reasons of efficiency and economy unrelated to taxes, principally to facilitate coordinated scheduling of deliveries of similar items to different contractors at three different sites.

In addition, for some years cost-type contractors of the Oak Ridge Operations Office have been authorized, as an economy measure and by arrangement with GSA and other Federal agencies, to issue delivery orders against supply contracts entered into by the General Services Administration and other Federal agencies for the acquisition of property for the Government, and to handle directly the payment of invoices for property delivered. Finally, the Oak Ridge Operations Office has long procured directly miscellaneous products and articles needed in plant operations which are produced by other divisions or subsidiary corporations of the plant operating contractor; although once the contracts were made delegations were given to the contractor to schedule deliveries, receive the property and make payment. In

both situations the Government obtains title to the property directly from the vendors and payment to the vendor is made from Government funds advanced to the contractors for this purpose.

In all of these cases, where significant amounts of taxes may be involved, instructions have been issued by the Oak Ridge Operations Office recalling the delegation to the contractors concerned to make payment for property delivered, and payment is now made by AEC through checks issued by Treasury disbursing officers.

With respect to all of the above arrangements, it is AEC's contention that the purchase was by the United States even though payment had been made by a contractor, so that the transaction was exempt either under the Federal Constitution or under state law. The purpose in recalling the payment authority granted to the Oak Ridge contractors and providing for direct payment through AEC was to eliminate any possible argument as to the availability of the constitutional or statutory exemption. The dollar amount of procurement transactions under the AEC contracts and other Government sources of supply affected by this action presently stands at approximately $342,000,000. The types of property being acquired under these contracts are process equipment for installation in the AEC-owned plants in Oak Ridge, Paducah and Portsmouth, such as compressors, tube sheets, converter shells and heads, evaporators, valves, meters, pumps, generators, heat exchanges, PG pipe and heavy electrical equipment; and under the GSA and other agency contracts gasoline and miscellaneous items of supplies.

The maximum sales and use tax (Tennessee and Ohio) on the above procurement actions is estimated as of the order of 8 to 10 million dollars. The gasoline tax which might have been payable in the absence of the revisions in procurement practices is estimated at approximately $100,000 for the next twelve months.

The recent actions taken by the Oak Ridge Operations Office in the interest of avoiding litigation and eliminating doubt as to the availability of tax exemptions would appear to be consistent with AEC's previous practice of procuring items directly where greater efficiencies or economics could thereby be achieved. Those actions have been taken only after examination of the particular situations involved and determination by AEC that such results could be achieved, taking into consideration any increased administrative costs to AEC and without impairment of contractor relationships. We are advised that to date the actions described have not required the hiring of additional personnel by AEC and have resulted in little, if any, additional administrative expense to AEC. Certainly, any increased administrative cost is negligible compared with the tax savings to be achieved.

The foregoing discusses actions taken by Oak Ridge Operations with respect to Ohio, Tennessee and Kentucky procurements. It is understood that similar actions have not been taken at other AEC installations, either because existing tax liabilities and exemptions based on state law were not affected by the repeal of the last sentence of section 9(b), or because the state has no sales and use tax, or because the tax situation is as yet unclear, or because the volume of purchases did not appear to warrant such action.

CONGRESS OF THE UNITED STATES
JOINT COMMITTEE ON ATOMIC ENERGY

December 23, 1953

Atomic Energy Commission
1901 Constitution Avenue
Washington 25, D.C.
Attention: Mr. Lewis L. Strauss, Chairman

Gentlemen:

I have received your letter of December 22 and the memorandum by your General Counsel.

I am sure that we are in accord in our desire to place the atomic energy program into normal commercial channels as soon as possible. I have read with interest, and with some confusion your statement that the General Manager directed the Managers of Operations:

> ". . . to procure materials directly and furnish them to subcontractors . . . ."

It would seem to me that this method of proceeding is against the intent of Public Law 262. It was the understanding of this Committee that the additional expense necessitated by Public Law 262 was approved by the Administration in advance as a necessary price for restoring, in small part, normal Federal-State relationships in this field.

I would appreciate receiving additional clarification.

Sincerely yours,

/s/ Sterling Cole
STERLING COLE
Chairman

EXHIBIT 22Q TO PLAINTIFF'S SUPPLEMENTAL ANSWERS TO DEFENDANTS' INTERROGATORIES (SECOND SET) 2/7/77 (R.V)

GOVERNMENT PROCUREMENT AND CONTRACTING (PART 2)

HEARINGS BEFORE A SUBCOMMITTEE OF THE COMMITTEE ON GOVERNMENT OPERATIONS HOUSE OF REPRESENTATIVES NINETY-FIRST CONGRESS FIRST SESSION ON H.R. 474 TO ESTABLISH A COMMISSION ON GOVERNMENT PROCUREMENT

MARCH 25, 26, AND 27, 1969

Printed for the use of the Committee on Government Operations

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WASHINGTON : 1969

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Then you go into the shipping industry and the Maritime Administration, and it is costing us around $700 million a year in subsidies. The Government pays 55 percent of the construction cost and 75 percent of the operating costs of the merchant marine. You can go on down the line into any phase of industry, and while all you hear from them is private enterprise and get the Government out of business, they would all commit suicide tomorrow if the Government got out of subsidizing —financial suicide.

Mr. Horton, you may pontificate for a while now.

Mr. HORTON. Mr. Chairman, I do not have any questions of Mr. Ramey.

AEC CONTRACTORS AS AGENTS

Mr. ROBACK. I do.

Commissioner Ramey, the AEC is unique in that atomic energy poses the most sensitive issues of Government control. Yet the whole procurement function is more widely delegated to industry, you might say, than in any other defense field.

Does that make the operating contractor more an agent of the Government than, let's say, a prime contractor for the Defense Department?

Mr. RAMEY. I would say in many cases, this is probably true. However, I would not classify the overall relationships as one of "agency" in the legal sense.

Mr. ROBACK. But he is on your side of the table?

Mr. RAMEY. That is right. We consider it is what we call a "partnership" arrangement where the operating contractor is working closely with the AEC management people, both the technical people and the procurement people so far as the operating contractor's procurement is concerned. So that we believe that it is close to being an agent but is not legally so. Some of the early contracts, for example, included language that said the con-

tractor is an independent contractor. The courts have taken in various positions on the matter of contractor relationship. Some of the big Defense Department contracts, especially these so-called incentive type, seem to be a little more of an "arm's length" kind of thing where the contractor is, at least theoretically, undertaking some risgs, for which he hopes to make some additional money.

Mr. ROBACK. And as part of that risk, he is hired to use his best judgment and his management skills.

Mr. RAMEY. That is right.

Mr. ROBACK. And here, while you want to have the same thing in one sense, you cannot let the contractor too far away on the tether.

Mr. RAMEY. That is right. We are trying to get the background, the business experience of the industrial or university contractor, but we recognize and he recognizes that the Government is assuming the risks and so we stay pretty close together.

Mr. ROBACK. So does this require or does it come about that you have more close supervision, comparatively, than, in the defense fields, and not only more close supervision, but more approval responsibilities?

SPECIAL CONTRACTOR RELATIONSHIPS

Mr. ROBACK. Well, in this rather special relationship which you have with the operating contractors, namely, that they collectively operate all the major facilities and, perform all the major substantive functions for the Commission, with the exception of these research contracts that you mentioned—

Mr. RAMEY. And there are certain other activities I might want to mention, like construction activities. We reserve a good part of the direct construction to AEC. On utilities, we utilize, of course, the GSA contracts for electric service. Sometimes there are major components which AEC directly contracts for. And, of course, on these demonstration reactor projects, again we contract for them directly with major participants.

Mr. ROBACK. But in all these other areas, the fact that a contractor, not the Government, is doing the contracting in a large way exempts these agencies legally from all procurement laws and regulations.

Mr. RAMEY. Not from all, but from some.

Mr. ROBACK. Not from all, but in a large way, I say.

Mr. RAMEY. Yes; at least, with respect to the procurement statutes.

Mr. ROBACK. So when you say you follow the practice of competitive bidding, you mean you try to follow it in the spirit of the law, but there is no obligation legally on the operating contractor in the same sense that there might be on the contracting officer in the Government.

Mr. RAMEY. For these activities, that is correct. On construction, for example, where AEC is handling this directly, we follow advertising and the straight out Government competitive bidding procedures. That is the area where the whole concept of advertising and formal advertising, and so forth, more or less grew up. So in this respect, we are like the Government generally and in these other aspects, where the contractor is subcontracting for research and development or for equipment, this sort of thing, you are right, he is not legally subject to all of the Government's procurement regulations.

Mr. ROBACK. Well, have you sorted out in your study which he is legally subject to and which he is not?

Mr. RAMEY. Yes, we have.

Mr. ROBACK. Will you supply a convenient summary or listing of that?

Mr. RAMEY. We have done this in the past and we are redoing it now as a result of this study group's review and report. We will be glad to provide you with the information as soon as it is finalized.

(See p. 462.)

COMPETITION IN SUBCONTRACTS

Mr. ROBACK. What information do you have—this question has been asked in the course of these hearings—

on the extent of advertised as against negotiated procurement carried on by your operating contractors?

Do you have any summary figures which would indicate the extent to which, for example, you have competition or advertised competition?

• • • • •

STIPULATION CONCERNING MEMORANDUM BY W. NOEL KEYES, (R.I-146-148)

IN THE UNITED STATES DISTRICT COURT FOR THE DISTRICT OF NEW MEXICO

Civil Action No. 75-418

UNITED STATES OF AMERICA, PLAINTIFF

vs.

STATE OF NEW MEXICO, ET AL., DEFENDANTS

STIPULATION

The parties hereby stipulate to the following matters of fact in the above-entitled cause:

1. In the course of preparing answers to defendant's interrogatories filed herein on July 26, 1967, counsel for plaintiff found in the files of the Office of Chief Counsel, Albuquerque Operations Office, ERDA, a document which was identified in plaintiff's answer to interrogatory 106, filed herein on February 7, 1966 (item (2), page 60), as "Memo Route Slip and attached memorandum dated November 13, 1959, from W. Noel Keyes, Counsel, Kansas City Area Office, AEC, to Chalmers C. King, Chief Counsel, Albuquerque Operations Office, AEC, subject: 'Ramifications of Utilization and Characterization of Bendix as an agent for the United States in its Activities under Contract 613.'" The Kansas City Area Office is a subordinate field office to the Albuquerque Operations Office. The document consists of 16 pages of what the United States characterizes as 'impressions, opinions and conclusions of the author on the stated subject", and which New Mexico characterizes as "legal analysis on the stated subject." The document nowhere states that it is an official statement of AEC legal or contracting policy.

2. Plaintiff asserted in its answer to interrogatory 106 and continues to assert that the document identified in

paragraph 1. above is privileged and not subject to production or disclosure pursuant to the Federal Rules of Civil Procedure in this litigation. By letter of March 11, 1977, to plaintiff's ccounsel, defendants' counsel asked if he could review certain documents identified in plaintiff's answers to interrogatories 18c and 106, as to which plaintiff had asserted a privilege, including the document referred to in paragraph 1, above, in order to determine "whether securing these documents would be of value or whether it would be a pointless exercise." By letter of March 13, 1977, counsel for ERDA responded on behalf of plaintiff that the documents could be reviewed by defendants' counsel at ERDA's offices in Albuquerque, New Mexico, subject to the understanding that "the Government is asserting a privilege with respect to these documents and that our making them available for your examination does not in any way constitute a waiver of privilege asserted."

3. In accordance with the understandings stated in paragraph 2., defendants' counsel reviewed all of the documents in question on March 24, 1977. By letter of May 4, 1977, defendants' counsel asked if plaintiff's counsel would stipulate to the existence of a very limited portion of the document identified in paragraph 1. In order to save both parties and the court the time and expense which might otherwise result from proceedings which would be required for the court to hear and determine the applicability and extent of the privilege previously asserted, plaintiff is willing to stipulate to the existence of such limited portion of such document, subject to the understanding that no claim of privilege previously asserted with respect to remaining portions of such document is thereby waived or relinquished by plaintiff.

4. The document identified in paragraph 1. contains the following statement by the author:

"The OR [Oak Ridge Operations Office, AEC] prime contract (1956 amendment) does not state that Union Carbide is an 'agent' of the U.S. (AEC Washington being adverse to use of the term in prime contracts at the time), but does specify that the corporation will manage in accordance with directives the AEC may give and procure when required 'on behalf of' the AEC."

The memorandum cites no authority or support for the above-quoted conclusion of the author.

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EXHIBIT 7

DIVISION OF CONTRACTS

REPORT OF STUDY OF ADMINISTRATION OF PROCUREMENT, ATOMIC ENERGY COMMISSION, 11/68, EXHIBIT 7 TO DEFENDANTS' CROSS-MOTION FOR SUMMARY JUDGMENT (R. III)

REPORT OF STUDY OF ADMINISTRATION OF PROCUREMENT AND CONTRACTING PROCEDURES OF MAJOR COST-TYPE CONTRACTORS

ATOMIC ENERGY COMMISSION

November 1968

* * * * *

1. It is not intended that this Volume be applied directly to contractor personnel engaged in procurement. Contractor personnel are governed by (1) applicable contract provisions and (2) procurement procedures established by the contractor and approved by AEC. It is intended, however, that the procurement practices and procedures as set forth in this Volume be made available to contractors as illustrative of the methods used by the AEC and for their consideration in the development or revision of their own written procurement practices and procedures. (Sec. 9101-16 AEC Procurement Manual, dated October 25, 1954.)

2. The FPR and AECPR shall be made available to the cost-type contractors that construct and operate AEC plants and laboratories as illustrative of the policies, practices, and procedures used by the AEC, for their consideration in the development or revision of their own written procurement practices and procedures. Cost-type contractors are governed by (1) applicable contract provisions and (2) procurement policies,

practices and procedures established by the contractor and approved by AEC. The FPR and AECPR will be employed by AEC in its review and approval of cost-type contractor procurement policies, practices and procedures. (9-1.104 (b) AECPR, dated July 1960.)

The Study Group was informed by the AEC that other statements had been issued to the effect that various policies and procedures included in procurement manual chapters or the AECPR should be made applicable to cost-type contractor procurement to the "maximum extent practicable" and "greatest possible extent," and that "managers shall assure that. . .", etc.

As a result, some AEC field offices believed themselves compelled to exert a maximum effort to bring major AEC cost-type contractors' procurement procedures into conformity with the FPR and AECPR. Also contributing to this belief was a statement by the Comptroller General in a letter of May 14, 1964 (B-152946), to the Chairman, AEC, that appropriate steps should be taken to ensure that future procurement by AEC cost-type contractors be conducted under procedures conforming, to the greatest extent practicable, to the Government's bidding standards.

In August 1964 the AEC undertook a major review of its operating policies and practices, including how closely the AEC should require its major prime contractors to follow AECPR and FPR in their procurement procedures. The staff committee, in its attempts to clarify the degree to which the FPR and AECPR should be applicable to cost-type contractor procurement, considered four possible alternatives:

(1) Make little change in the then existing system except to explain the meaning of such terms as "maximum extent practicable" and "greatest extent feasible."

(2) Consider the contractors as agents of the Government and require that they follow strictly the FPR and AECPR in their procurement activities.

(3) Completely eliminate from the AECPR all reference to their applicability to contractors, thereby clarifying that AECPR and FPR apply only to direct AEC procurement. The subcontract and purchase-order clauses of prime contracts would include a statement of the basic procurement policies to be followed by the contractor.

(4) Issue a new AECPR (Subpart 9-1.52, Procurement by Cost-Type Contractors) which would replace all previous general guidance concerning the applicability of the FPRs and AECPRs to cost-type contractor activity. In addition, identify specific provisions in the FPR and AECPR which the contracting officer is required to bring to the attention of cost-type contractors as constituting areas which require "appropriate treatment" in the development of statements of contractor procurement practices.

The last of the above alternatives was adopted in May 1965 in an attempt to eliminate the confusion previously experienced as a result of such phrases as "to the maximum extent practicable" and "to the fullest extent practical." Consistent with the objective of retaining contractor flexibility the AEC's action was apparently intended to reduce the possibility of contractors' being held to the same precise procedural requirements as are stipulated for direct AEC procurement. However, this intent was not made clear in the transformation of the policy statement into procurement regulation language. In addition, the "appropriate treatment" concept as it is being interpreted and applied by certain AEC Field Offices results in an inflexibility that is not consistent with this intent.

The lack of clear understanding of what was intended by "appropriate treatment" became apparent to AEC Headquarters. Commissioner James T. Ramey, in an address to a meeting of the AEC Operations Office Managers in March 1967, stated:

EXHIBIT 22-L TO PLAINTIFF'S SUPPLEMENTAL ANSWERS TO DEFENDANTS' INTERROGATORIES (SECOND SET) 7/7/77 (R.V)

UNITED STATES ATOMIC ENERGY COMMISSION

Ninth Semiannual Report

of the

ATOMIC ENERGY COMMISSION

[SEAL]

January 1951

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* * * * *

III

ADMINISTRATION OF ATOMIC ENERGY CONTRACTS

To administer the contracts through which the various atomic energy operations are carried out, the Atomic Energy Commission some times has had to find new ways for Government and industry to work together, and to develop management devices not previously used in Government programs.

This is more generally true of cost-reimbursement contracts, but even in administering lump-sum and unit-price contracts, AEC has responsibilities not ordinarily found when contractors undertake to provide specified suppliers or services to the Government at a fixed price. The descriptions of contract provisions and devices in the previous chapter underscored some of these: maintenance of security protection of workers' health, and the public against special hazards and accountability for atomic energy materials.

Where contracts are for operating facilities in the fissionable materials production chain, AEC must closely schedule output and take every necessary precaution against delay of work. The unit-price production contracts, found in the feed materials operations call for periodic redetermination of price (p. 45), and AEC must therefore review costs of such contractors to an extent not usually necessary in fixed-price contracting.

Cost-Reimbursement Contracts

It is in the administration of cost-reimbursement contracts, however, that the management problems most characteristic of the atomic energy program are met with. The firms operating large Government-owned production plants, carrying on extensive development projects, and undertaking urgent construction jobs, work in close day-by-day cooperation with the Commission and its staff. They have been selected for their competence, and the Government is contracting with them not only for technical ability but for managerial ability as well. The working relationships between the Commission and its operating contractors resemble in some aspects those between industrial companies and their branch offices. The contractor undertakes to carry on an extensive operation; the Commission establishes the objectives and makes the decisions required to fit the operation into the national program, and exercises the controls necessary to assure security, safety, desirable personnel administration, and prudent use of the public funds.

Of the many administrative innovations required to make possible this kind of relationship between a Government agency and a number of industrial concerns, those in the field of finance are fundamental.

AEC Finance

The financial procedures in use in the atomic energy enterprise in 1947 when the Commission took office were

the traditional Government system employed during the war emergency and were not specifically designed for industrial operations like the atomic energy program.

The record-keeping practices and audit prodecudes, in line with Government requirements, were intended primarily to provide the Government with justification of the cash expenditures under their contracts, item by item. These methods did not provide the up-to-date meaningful records of costs and the adequate basis for financial control of property so essential in the management of industry. The general accounts did not reflect the difference between capital and operating expenditures. They did not recognize the existence of such items as year-end accruals, inventories, and other factors necessary for preparing meaningful financial reports. They were not adapted to development of the accounting data necessary to provide the essential basis for sound management.

The customary procedure in the audit of certain contracts was resulting in a triple item-by-item voucher check—first by the contractors' employees, then by AEC staff, and finally by auditors of the General Accounting Office. The real purpose of an audit was lost in a mass of papers. Instead of giving the entire operation a critical review for general conformity with the purposes of the contract and with generally accepted standards for internal control and good accounting practices, the audit consisted primarily of a recalculation of items supporting contractors' expenditures. The sheer volume of paper work incident to the detailed pre-audit of reimbursements to contractors caused irritating delays. Reconciliations of contractors' records with those ofg AEC were unnecessarily difficult.

Cost of the Work the Basis for Accounting

In developing a system better suited to its needs, AEC has had the support of the Congress and the Bureau of the Budget, the General Accounting Office, and the Treasury Department. By July 1948, AEC had developed and

was beginning installation of accounting and financing systems designed to fit its Government-contractor operations with all their industrial ramifications. By the spring of 1949, enough accounting data were available to permit AEC to draw up a budget request for proposed fiscal year 1951 activities in terms of the costs of performing the work to be done; that is, it had what the Hoover Commission has designated a "performance" budget, based on costs by functions rather than simply on the cash expenditures required. AEC in 1949 recast its 1950 budget in terms of the costs of the activities and has now had a complete year of experience with the cost-based performance budget.

A report on the accounting support of the budget of the various Government agencies, prepared by special survey teams at the request of the Hoover Appropriations Committee, contains the following AEC system:

> Except for agencies under the Government Corporation Control Act the AEC was the first Federal agency to adopt both an industrial-type accouning system and the cost-based performance for all of its operations. In view of the increasing interest in the use of industrial accounting principles for Government agencies, it should be pointed out that the Commission possesses two of the essentials without which the full benefits of such a system cannot be realized; appreciation by management of the value of a good accounting system, and recognition of the need for an adequate accounting organization manned by qualified personnel. In the installation of the new system, which began in 1948, AEC has had the active cooperation of the GAO-Treasury-Budget Bureau Joint Accounting Program. The accounting principles employed have been approved by the Comptroller General.

The accounting is well integrated with budgetary preparation and execution. The activity classification and the cost accounting records and reports together constitute an effective tool for the financial and general management of operations. Its usefulness should increase as AEC refines its systems and gains experience in their use.

"Integrated" Contractors

The basic concept that has made possible the development of such a system in a contractor-operated Government enterprise is that of the 'integrated" contractor. For accounting purposes, major cost-type contractors are treated as though they were branch offices and the AEC the home office. Under this arrangement AEC generally advances funds to its major cost-type contractors and then holds them responsible for a proper accounting. The contractors' financial and accounting operations under AEC contracts are required to be clearly separated and departmentalized from their other activities. The contractors maintain "branch" books of account and internal controls for AEC operations that are in conformity with generally accepted accounting principles and approved by the Commission. Contractors' accounts thus become an integral part of the AEC accounting system.

The contractor submits comprehensive monthly financial statements to AEC showing the financial results of contract operations. AEC periodically conducts examinations of the contractors' accounts and procedures for work under the AEC contracts, similar to the examinations performed by public accountants in the certification of financial statements. The result is to eliminate duplication of audit work and serious delays in reimbursement to contractors.

AEC's major cost-reimbursed operating contractors and most large contractors for development work are "integrated" in this way. Examples are the Carbide &

Carbon Chemicals Division of the Union Carbide & Carbon Corp., the Nucleonics Department of the General Electric Co., and the Atomic Power Division of the Westinghouse Electric Corp. The salient points concerning accounting and financing under one of these AEC contracts are as follows:

a) Contract operations are financed from funds advanced to this contractor by the Commission and deposited in a special bank account.

b) Payments from these funds are audited periodically by AEC.

c) A separate and distinct set of accounts is set up and maintained to provide detailed data both by operating units of the contractor's organization and by AEC activities. Thus, the contractor and AEC can consolidate data as needed by each with comparable data for other operations.

d) Contractors' methods of handling payrolls, procurement, and stores have been adopted in general, with only slight modification to meet AEC requirements.

e) The contractor accounts for all funds, property, and facilities furnished to the activity. Accounts are audited by AEC and the General Accounting Office.

f) Periodic and special financial and operating reports are available to provide the basis for management and budgetary decisions.

Nonintegrated Accounts

There are numerous cost contractors whose accounts are not integrated with those of AEC, generally those with contracts involving relatively small sums of money or short periods of time. Even some large cost-type construction contracts, because of their limited duration, are not accounted for on an integrated basis. In such cases,

AEC reviews the contractor's accounting procedures in advance to assure that they will provide the cost data necessary for the maintenance of AEC accounts.

AUDITING

The installation of a modern industrial-type accounting system with provisions for internal controls made necessary the adoption of modern auditing techniques patterned after the methods of the public accounting profession. The primary aims of this type of examination are to see that funds and property are adequately protected by systems of internal controls and to establish the integrity of the financial statements. The audit includes the examination and verification of assets, liabilities, income, expenses, and cost distributions. Supporting documents are checked only to the extent necessary to determine the adequacy and accuracy of the general records. The accounting and internal control systems are reviewed to determine whether they are adequate to provide reasonable safeguards over assets, and furnish accurate and reliable information. The major improvement in the over-all audit program represents another instance in which AEC has adapted commercial methods to its operations.

Three Phases of the Audit

Where the accounts of a contractor are integrated with the AEC accounting system, the audit by AEC generally has three phases. A reimbursement audit is performed primarily to verify the contractors' net expenditures for approval of reimbursement or recoupment vouchers. Interim examinations are made from time to time during the year to test the adequacy of accounting records and internal controls. These examinations are a part of a comprehensive audit customarily completed once a year to verify the balance sheet and operating statements of the contractor.

Examinations and reviews independent of the comprehensive audit are made of financial operations under the various provisions of all contracts. In addition to verifying the correctness of the related financial transactions, these reviews provide valuable information to management and reveal ways of improving procedures and tightening controls.

The audit branches in operations offices are under the administration of the directors of finance and are independent of the accounting branches. Auditors from the Washington Office conduct on-the-site reviews of operations office audits and also review the copies of audit reports sent to the AEC controller.

GAO Audits

The General Accounting Office has cooperated with AEC in all of its auditing problems. In accordance with an agreement with the Comptroller General in October 1947, the GAO Audit Division has a staff stationed at each major AEC site. Since most contractors' records are now examined at the site by both AEC and GAO, the problem of duplicate records is largely eliminated. Both the contractors' records and the AEC audit reports and working papers are available at all times to the GAO aduitors. The GAO Corporation Audits Division is now starting a comprehensive audit of AEC accounts.

Accounting and Contract Administration

The AEC accounts have been established in the exact pattern of the work to be done throughout the enterprise; that is, the divisions and subdivisions of the budget and reporting classification are the same as the divisions and subdivisions of the operating program. Thus the making of the budget (estimation of future costs) is inseparable from program planning, and the accrual and periodic reporting of costs incurred is the basis for progress reporting as the program is carried out.

The budgeting and accounting systems provide one of the means through which AEC and its contractors jointly plan the jobs ahead, dividing and subdividing the major objectives into specific activities for which cost estimates are prepared. Similarly, in the execution of the programs, the contractors' periodic cost reports, along with their reports of physical work accomplished, make possible the continual measurement both of work done in relation to schedule and costs in relation to estimates. At the same time these reports provide the basis for planning the work ahead.

Contract Administration

Underlying the relationship of AEC to its major cost-reimbursed contractors—whether they be contractors for plant operation, laboratory operation, development, or construction—there are certain mutually recognized principles growing out of AEC's basic policy for contractor operation and method of selecting contractors. Briefly, they are:

a) The contractor recognizes that the AEC is responsible under the law for the conduct of the atomic energy program.

PLAINTIFF'S ANSWER TO INTERROGATORY 9, PLAINTIFF'S SUPPLEMENTAL ANSWERS TO DEFENDANTS' INTERROGATORIES (SECOND SET) 2/7/77 R.IV)

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9. As to ZIA, LACI and Sandia, state whether it is your contention that the contractor is an agent of the United States:

a. For all functions under its contract;
b. For some functions under its contract;
c. For no functions under its contract.

SUPPLEMENTAL ANSWER: Plaintiff's original answer to interrogatory number 9 fully explains plaintiff's contentions in this litigation with respect to the "agent" status of its management contractors. It is plaintiff's position that no further answer is required under FRCP Rule 33. However, it is plaintiff's desire to explain its position on all issues to the fullest extent possible, and plaintiff will endeavor to do so on the subject of interrogatory number 9 in this supplemental answer. This endeavor is made difficult by the fact that the interrogatory does not explain what defendants consider to be "functions under" the contracts or enumerate any such "functions." Nor does the interrogatory define the term "agent," which term, like the related terms "servant" and "independent contractor," has been difficult for authorities in the field of agency law to define with precision.

Traditional legal terminology in the field of agency law was fully developed before the emergence of the AEC's management contract concept in the 1940's. Therefore, it is understandable that the relationship contemplated by the management contract concept is not always accurately or completely described by the imprecise labels of the traditional terminology.

In this supplemental answer, plaintiff has taken into account the following authoritative statements with respect to the term "agent" and other related terminology of the traditional law of agency:

"Because of their brevity, definitions are more or less incomplete and inaccurate." (Seavey, *Law of Agency* § 1 (1964).)

"The brevity of a definition necessarily makes it an incomplete and inaccurate statement." (Restatement of Agency (Second), Introductory Note to Topic 1, Definitions.)

"Agency is the fiduciary relation which results from the manifestation of consent by one person to another that the other shall act on his behalf and subject to his control, and consent by the other so to act." (Restatement of Agency (Second) § 1.)

"It is also generally recognized that the relationship of principal and agent may arise by operation of law." 3 Am. Jur.2d Agency § 19.

"The agency relation exists in order to enable a person to utilize the services of others and thereby to accomplish what he could not achieve alone." (Seavey, *Law of Agency* § 2 (1964).)

"This power is the characteristic result of the agency relation—the ability of the agent to subject the principal to personal liability and to create rights in his favor." (Seavey, *Law of Agency* § 3 (1964).)

"A servant is an agent who agrees to devote his time to his employer's business or family affairs and whose physical conduct, in the scope of employment, the employer normally has a right to control. As with all brief statements of rules, this statement only approximates accuracy. It is sometimes said that the right to control his physical activities is the test; while this is important, it is not always essential." (Seavey, *Law of Agency* § 6 (1964).)

"For agency purposes, any one who acts for, or contracts with, the principal other than as a servant, is

> an independent contractor. The category includes agents who are authorized to make contracts for the principal and also persons who are not agents but who have agreed to do things or accomplish results which the principal desires, with or without pay. In other words, there are two kinds of independent contractors—those who are agents and those who are not." (Seavey, *Law of Agency* § 6 (1964).)
>
> "Independent contractor' is used as a term to indicate someone employed but who is not a servant of the employer. As stated in Section 6, while the term is antithetical to the term servant, all agents except servants fall within its meaning. The distinction between agents who are servants and those who are independent contractors is important only in cases involving the liability of the employer for the physical acts of the one employed." (Seavey, *Law of Agency* § 10 (1964).)

As stated in plaintiff's original response to interrogatory 10, the relationship between ERDA and its management contractors "contain elements of the master-servant, principal-agent, and principal-independent contractor relationships." A given "function under" the contract, whatever the term entails, will probably contain elements of more than one of the relationships, as defined, with no real precision, in the terminology of the traditional law of agency.

The basic reason underlying AEC's use of management contractors is the same reason which underlies the typical principal-agent relationship. As stated in the legislative history of the Atomic Energy Act of 1946, the Act "permits management contracts for the operation of Government-owned plants so as to gain the full advantage of the skill and experience of American industry." (S. Rept. 1211, 79 Cong. 2d Sess. 15 (1946). See Exhibit 22-L at p. 39, Exhibit 22-P at p. 70 and Exhibit 22-AI.) Through management contractors, AEC and ERDA have not

merely purchased goods and services, but have carried out their own functions as Government agencies under the Atomic Energy Act.

The term "independent contractor" is also an accurate description of some aspects of the relationship. ERDA and AEC have not undertaken to direct the details of day-to-day operation, which would be contrary to the management contract philosophy. Instead, ERDA directs the general areas of work to be pursued and the results to be obtained. There are "functions," however, in which the term "servant," although imprecise, accurately describes aspects of the legal relationship between ERDA and one of its management contractors (e.g., the protection and safeguarding of Government property and classified material). There are other functions where "independent contractor" is a more appropriate label than "servant."

Regardless of whether a management contractor is predominantly a "servant" or predominantly an "independent contractor" for a given "function under" the contract, an essential aspect of agency is always present. This essential element of agency is the ability or power of the management contractor to create obligations of the Government, payable directly from Government funds. This power or ability has been described as the "characteristic result of the agency relation." (Seavey, *Law of Agency, supra.*) This essential element of agency is present with respect to *all* functions under the contract which ultimately result in the incurrence of obligations of third parties and the making of payments to obligees from Government funds. Thus, while the management contractor may be an "independent contractor," rather than a "servant" for a given "function under" the contract (e.g., directing the details of day-to-day research or maintenance operations and the hiring and direct supervision of employees), the management contractor is also properly labeled "agent" for these functions to the extent that they result in the incurrence of obligations

(e.g, the salaries of employees) payable directly from Government funds.

With respect to the "function" of procurement of tangible personal property, there are additional indicia of agency present. Not only is the Government's money used and a Government liability created when the purchase order is issued, but also, title and ownership of the property pass directly to the Government. Furthermore, such purchases are subject to prior approval of ERDA, are made in accordance with procurement procedures approved by ERDA, and are subject to certain specified provisions of the Federal Procurement Regulations and ERDA Procurement Regulations.

On the basis of the foregoing, plaintiff responds to the interrogatory by stating that the contractors have the essential attributes of "agents" with respect to all "functions under" the contracts which result in the expenditure of Govenment funds in furtherance of Government operations in Government facilities under their respective contracts.

Plaintiff admits that the basic contract documents at issue in this case do not use the term "agent" to describe the relationship between ERDA and its management contractors. Plaintiff contends that "agent" is an accurate description of the relationship to the extent stated above. However, plaintiff will contend that the real issues in this case—whether the Government is the purchaser and the owner of the funds used in operations—can be

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PLAINTIFF'S ANSWER TO DEFENDANT'S INTERROGATORY 10, 8/31/76 (R. IV)

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10. If your answer is that one or more of the contractors is an agent of the United States only "for some functions under its contract", state with particularity all functions for which such contractor(s) is not an agent and the extent and limits of such functions.

ANSWER: Virtually all functions performed by ERDA management contractors take on some aspects of "agency" because all such functions are devoted exclusively to the execution of Government programs in Government-owned facilities with all costs and expenses paid for directly from Governme.t funds. The term "agent," however, is an imprecise term with a variety of attributes and legal consequences flowing from its use, depending and the context. In the general context of an AEC management contract, plaintiff contends that the following is an accurate statement:

> "The exact legal relationship under the management contract concept is difficult to define in traditional legal terminology. The AEC-management contractor relationship is unique. It contains elements of the master-servant, principal-agent, and principal-independent contractor relationships. These ordinary legal classifications, however, are inadequate to identify accurately the relationship existing under the long-term arrangements utilized for conducting AEC's operations and have caused problems in a variety of legal areas. . . .
>
> "In general, there was no preconceived position as to what the legal relationship should be, or what either the tax or other legal consequences might be. The legal questions generated have been the natural consequences of the different interests affected by particular circumstances or actions, political considera-

tions, and the ingenuity of lawyers." Hiestand and Florsheim, *The AEC Management Contract Concept*, 29 Fed. B.J. 67, 75, 78 (1969).

Plaintiff admits that it has been argued on occasion that management contractors are "independent contractors" so that negligence on the part of contractor employees should not provide a basis for liability of the Government under the Federal Tort Claims Act, 28 U.S.C.A. §§ 1364(b), 2671, *et seq.* Plaintiff denies that "agent" and "independent contractor" are mutually exclusive terms. Plaintiff admits that employees of management contractors are not Government employees.

11. As to contracts between ERDA/AEC and Western, Zia, LACI or Sandia at any time between 1946 and the present time, state all instances in which any such contracts, or documents in force during the term of such contract, explicitly designated a contractor as an "agent" of the government in any way, empowered a contractor to act "on behalf of" or "for the account of the government or "bind the government in contract" in any way, or stated that the government "deemed itself bound by actions of the contractor" in any way, or "would guarantee payment to a supplier of the contractor" in any way or utilized language equivalent to that set out in quotations marks in this * * *

ANSWER TO INTERROGATORY 10, PLAINTIFF'S SUPPLEMENTAL ANSWERS TO DEFENDANTS' INTERROGATORIES (SECOND SET) 2/7/77 (R. IV)

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8. State whether it is your contention that Zia, LACI or Sandia are "instrumentalities" of the United States as that term is used by the Supreme Court in *United States* v. *Boyd*, 378 U.S. 39 (1964). If your answer is in the affirmative, state as to each contractor for whom a claim of instrumentality is made,

a. The names and occupational affiliation of each member of the contractor's board of directors and whether such contractor's board of directors includes officers or employees of the United States;

b. Whether such contractor's officers include officers or employees of the United States;

c. Whether such contractor is chartered by Congress;

d. All ways in which such contractor differs in structure, function and affiliation with ERDA from the contractor in the *Boyd* case;

e. The names of the persons or entities holding each contractor's shares and the number of shares each person or entity holds. *SUPPLEMENTAL ANSWER*: For purposes of this supplemental answer, the interrogatory is, in accordance with plaintiff's letter of September 24, 1976, considered a request for an admission "that the contractors [Zia, LACI, and Sandia] are not 'instrumentalities' within the meaning of *Department of Employment* v. *United States*, 385 U.S. 355 (1966)."

Plaintiff admits that Zia, LACI and Sandia do not meet all of the criteria for an "instrumentality" which were enumerated by the Supreme Court in *Department of Employment* v. *United States*, 385 U.S. 355, at page 359. However, plaintiff contends that ERDA has a relationship with Sandia Corporation which is unique among management contractors in light of the matters

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set forth in paragraphs 2 and 3 of the Ross affidavit and in Articles I, II, III, V and Appendix A of Contract AT(29-1)-789, Exhibit 3 to the Roser affidavit, all of which were submitted in support of plaintiff's motion for summary judgment. Plaintiff contends that this special relationship, though not strictly meeting the criteria of "instrumentality" in *Department of Employment*, is closely akin to an "instrumentality" type of relationship in light of those special aspects of the ERDA-Western-Sandia relationship to which reference has been made herein and in plaintiff's original answer. Plaintiff contends that these "instrumentality" features, while not essential for plaintiff to prevail, do place Sandia in a special category with respect to the issues raised in this litigation.

EXHIBIT 114-A TO PLAINTIFF'S SUPPLEMENTAL ANSWERS TO DEFENDANTS' INTERROGATORIES (SECOND SET) 2/7/77 (R.V)

United States Atomic Energy Commission

FIFTH SEMIANNUAL REPORT OF THE ATOMIC ENERGY COMMISSION

January 1949

UNITED STATES GOVERNMENT PRINTING OFFICE
WASHINGTON, D.C. — 1949

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FINANCE

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ACCOUNTING AND AUDITING METHODS

In wartime, in the field of atomic energy, many unusual arrangements were utilized. One of the most difficult tasks facing the Commission was to obtain a clear picture of those arrangements in order to have the background necessary for sound decisions on accounting and methods of handling funds. In the fall of 1947, the Commission decided to employ public accounting firms, under contract, to review and evaluate accounting practices under typical contracts taken over from the Manhattan project.

REVIEW OF ACCOUNTING AND AUDITING METHODS

After consultation with the Comptroller General, the Commission contracted with the following public accounting firms for the review:

Haskins & Sells.
Lybrand, Ross Bros. & Montgomery.
Scovell, Wellington & Company.
Arthur Andersen & Company.
Touche, Niven, Bailey & Smart.

Each firm was assigned one of the five typical contracts selected for review. These contracts represented a cross section of Commission activity, covering town management, research, plant construction, and production. The public accountants reviewed the accounts and records of both the contractor and the Government under the selected contracts. Each firm worked independently of the others, and each made a separate report of its findings.

Extensive Revisions Necessary

Before the end of January 1948, the Commission had received the reports of the accounting firms, covering the accounting policies, standards, and procedures prevailing under the various contractual arrangements reviewed. The accounting firms had worked on different types of contracts, yet their findings had a similarity that left no doubt that extensive revisions were necessary before the accounting records and procedures and the methods of internal control instituted in wartime could be considered adequate for the Commission's long-term peacetime conditions of operation.

The record-keeping practices and audit procedures that the contractors had previously followed were primarily designed to justify their expenditures to the Government, item by item. But these methods did not serve the functions so essential in the industrial and commercial world, of providing up-to-date meaningful records of costs and controls of property. Changes were needed to eliminate duplication of audit work and records, to speed up reimbursement of contractors, and to arrive at complete and realistic operating statements.

The accountants' reports confirmed rather completely the opinions developed by the Commission's staff, that the only practical solution to the accounting problems lay in a fundamental departure from the conventional Government accounting concepts and practices.

REVISION OF ACCOUNTING AND AUDITING METHODS

Government agencies generally have considered that the Government's accounting begins when the Government disburses funds. Their general practice when operating through private contractors on a reimbursable-cost basis, has been to record the initial sums paid such contractors as advances and to reflect costs in the Government's accounts only when contractors' expenditures have been audited and reimbursed by the Government. This practice has two basic weaknesses in the accounting for contract activities of the nature of the atomic energy program:

(1) A considerable lag in time exists between the dates when the contractor incurs costs and when the Government accounts record the expenditures.

(2) It is extremely difficult for the Government to break down the records of these expenditures so as to obtain a useful costs analysis—how much has been spent for any particular purpose at any particular time.

Much time and effort has been spent in the past in auditing the details of these reimbursements and attempting to analyze them in terms of intelligible costs.

Contractors' Relation to Government

In studying this matter, the Commission's accounting staff realized that for accounting purposes the major cost type contracts should be considered as though they were to use a business concept—affiliated corporations as far as their contracts with the Commission were concerned. Costs would thus be considered as incurred by the Government at the moment the contractors incurred them, and the movement of cash between the Government and its contractors should have no more cost-accounting significance than the transfer of funds from one bank account to another.

Auditing and Financing

If Commission contractors established separate sets of accounts for their operations under the contracts, kept Commission funds separate from their own, and maintained adequate systems of internal control and pre-audit on the expenditure of these funds, under Commission direction, it would become unnecessary for the Commission to subject such contractors' expenditures to the detailed item-by-item examination of the conventional Government type. For this examination, the Commission could substitute a comprehensive field audit—such as would be performed by a public accounting firm in the examination of the accounts of any business.

By eliminating the cumbersome reimbursement procedure under which all the detailed transactions are individually audited before reimbursement, the Commission could furnish funds to the contractor as promptly as required. Contractors could then operate with a smaller working fund advance.

Comprehensive Accounting

By treating cost-type contractors as operating affiliates for accounting purposes and subjecting their contracts, accounts, and statements to periodic commercial-type audits, it becomes possible, under the new system, to adopt the accounting techniques of intercompany accounts and consolidated statements. The Commission establishes "intercompany" accounts on its books for cost-type contractors to charge them with all funds, facilities, and material provided them. The contractors keep similar accounts to credit the Commission with these items. Customary asset, liability, and operating accounts are maintained by contractors. From these accounts they prepare monthly financial and cost statements, which the Commission uses in preparing consolidated statements for the entire program. This makes unnecessary all attempts to obtain costs by analyzing contractor's reimbursements.

INSTALLATION OF NEW ACCOUNTING METHODS

Simple and almost obvious as these concepts may appear, the practical application of them to a going concern of the magnitude of the Commission's extensive and diversified operations has added up to a considerable task. The Commission has enjoyed the wholehearted support and assistance of the Comptroller General of the United States and his staff in instituting the new accounting policies. Adopting the commercial-type audit at the contractor's site in lieu of the voucher-type of reimbursements has posed some technical difficulties which have temporarily delayed realization of the full benefit to be derived from the new approach. Here again, Comptroller General Warren has shown great interest and helpfulness in working out these problems.

Contractors, for the most part, have received these new procedures with approval. The procedures made sense to industrial contractors, as well as to the public accountants consulted, because they are pat * * *

EXHIBIT 14

ERDA-PR TEMPORARY REGULATION NO. 17, 4/2/76, EXHIBIT 14 TO DEFENDANTS' CROSS-MOTION FOR SUMMARY JUDGMENT (R.III)

UNITED STATES
ENERGY RESEARCH AND DEVELOPMENT ADMINISTRATION
Washington, D.C. 20545

April 2, 1976

ERDA-PR TEMPORARY REGULATION NO. 17

SUBJECT: ESTABLISHING AND NEGOTIATING PROFITS AND FEES

1. *Purpose:* This regulation establishes ERDA profit/fee policy.

2. *Effective date:* This regulation is effective upon publication in the *Federal Register.*

3. *Expiration date:* This regulation will remain in effect until it is canceled or until its provisions are incorporated into the ERDA-PR.

4. *Explanation of changes:*

Delete subsections 9-3.808-50 and 9-3.808-51 and add the following section 9-3.808 and new subsection 9-3.808-50, 9-3.808-51 and 9-3.808-52:

§ 9-3.808 *Profit or fee.*

§ 9-3.808-1 *General.*

(a) A fair and reasonable provision for profit or fee is called a profit objective. The profit objective, when combined with the estimated cost of contract performance, becomes the contract price objective the ERDA negotiator takes into negotiations with a contractor. The profit

objective is an amount which, in the judgment of the ERDA negotiator, is appropriate for the procurement. The price objective should be reasonable in relation to the task to be performed and the requirements placed on the contractor.

(b) ERDA's policy is to: reward contractors who undertake more difficult work requiring higher skills; allow contractors the opportunity to earn profits commensurate with the cost risk they are willing to assume—the greater the risk, the higher the profit objective; reward contractors who have excellent records of performance; and reward contractors who provide their own facilities and financing or who have established their competence through prior research or development work undertaken at their own risk.

(c) The profit objective will be determined individually for each contract. Across-the-board agreements as to rates of profit or fee will not be made. The determination of a fair and reasonable profit or fee is a matter of sound business judgment.

§ 9-3.808-2 *Factors for determining profit or fee.*

(a) The factors in FPR § 1-3.808-2 will be used in establishing profit objectives. However, if the work is to be performed in commercial facilities, the weighted guidelines technique in § 9-3.808-50 will be used in place of those factors when the contract is estimated to exceed $500,000, and may be used on contracts below that figure.

(b) The amounts payable as fees on contracts for operation of Government-owned facilities, for construction and for performance of on-site support and architect-engineering services will not exceed maximum amounts derived from the appropriate fee curve set forth in the interim ERDA Profit and Fee Handbook (March 1976). Requests to pay fees in excess of the maximum will be sent to the Director of Procurement, ERDA Headquarters.

§ 9-3.808-50 *Weighted guidelines.*

(a) Weighted guidelines is an analytical technique that requires consideration of the relative value of appropriate profit factors in establishing a profit objective and conducting negotiations. It also provides a basis for justifying the objective and explaining any significant departure from the objective in negotiating a final agreement.

(b) Analysis of weighted guideline factors is done using information available in proposals, audit reports, performance appraisals, preaward surveys and the like. No more data on or analysis of costs is required to establish a profit objective than is required to determine reasonable estimated costs.

(c) If use of weighted guidelines results in a profit objective in excess of limitations established by statute or regulation, the percentage allowed pursuant to such limitations shall be the profit objective. No local administrative ceilings may be placed on profit or fee.

(d) The factors set forth below shall be used in applying weighted guidelines. The weight ranges listed after each factor shall be used in all instances.

Profit Factors	Weight Ranges
Contractor's Input to Total Performance	
Direct Materials	
Purchased parts	1 to 4%
Subcontracted items	1 to 5%
Other materials	1 to 4%
Engineering labor	9 to 15%
Engineering overhead	6 to 9%
Manufacturing labor	5 to 9%
Manufacturing overhead	4 to 7%
General and administrative expenses	6 to 8%
Contractor's Assumption of Contract Cost Risk	0 to 7%
Type of contract	
Reasonableness of cost estimate	
Difficulty of contract task	

Profit Factors	Weight Ranges
Record of Contractor's Performance	−2 to +2%
Small business participation	
Management	
Cost efficiency	
Reliability of cost estimates	
Timely deliveries	
Quality of product	
Inventive and developmental contributions	
Labor surplus area participation	
Selected Factors	−2 to +2%
Source of resources	
Governmental or contractor source of financial resources	
Special achievement	
Other	
Special Profit Consideration	0 to +4%

(e) Use of the weighted guidelines method of profit analysis is discussed in detail in the interim ERDA Profit and Fee Handbook (March 1976).

§ 9-3.808-51 *Contracts with not-for-profit organizations (other than educational institutions).*

(a) It is general ERDA policy to pay fees in contracts with not-for-profit organizations; however, it is a matter of negotiation whether a fee will be paid in a given case. In making this decision, consider whether the contractor is ordinarily paid fees for the type of work involved. No fees will be paid when the contract involves a cost sharing arrangement.

(b) Where the contract with the not-for-profit organization is for the operation of Government-owned facilities, calculate fees using the procedures and schedules applicable to operating contracts set forth in the interim ERDA Profit and Fee Handbook (March 1976). Where the contract work is to be performed in the contractor's

privately-owned facilities, calculate fees using weighted guidelines.

(c) In computing the amount of fee to be paid, take into account the tax posture of the not-for-profit organization. While it is difficult to establish the degree to which a fee under any given contract contributes to an organization's overall net profit, assume that there is an element of profit in the fee paid.

(d) In order to assure consideration of the tax posture of not-for-profit organizations during fee negotiation, calculate the fee as for a contract with a commercial concern and then reduce it at least 25%. However, depending on the circumstances, contracting officers may pay fees somewhere between this amount and the fee allowable if it were a commercial concern. When this is the case, document the contract files to specifically state the reason or reasons.

§ 9-3.808-52 *Contracts with Educational Institutions.*

(a) It is ERDA policy not to pay fees under contracts with educational institutions.

(b) However, some university contractors operate Government-owned laboratories essentially apart from and not in conjunction with their other activities and the complexity and magnitude of the work are not normally found in university contracts. If, in these cases, the parties are not able to agree as to the amount of central university indirect expenses for purposes of reimbursement under the contract, it is permissable to pay a "management allowance", which, where necessary, may exceed ERDA's conservative estimate of anticipated central indirect expenses. However, the amount may not exceed the university's estimate of properly allocable central indirect expenses or the fee developed using the weighted guidelines, whichever is lower.

(c) As noted above, the payment of a management allowance can be justified only under special circumstances; accordingly, such arrangements shall not be

negotiated without the prior approval of the Director of Procurement.

5. *Authority*: Section 105 of the Energy Reorganization Act of 1974 (P.L. 93-438).

/s/ Robert F. Allnutt
ROBERT F. ALLNUTT
Acting Director of Procurement

EXHIBIT 13-B TO PLAINTIFF'S SUPPLEMENTAL ANSWERS TO DEFENDANTS' INTERROGATORIES (Second Set) 2/7/77 (R.V.)

PAYMENTS TO STATE OR LOCAL TAXING UNITS

* * * * *

EXCERPT OF A LETTER FROM R. C. LANPHIER, JR., DEPUTY ASSISTANT SECRETARY OF DEFENSE (SUPPLY AND LOGISTICS), TO HON. ROWLAND HUGHES, DIRECTOR, BUREAU OF THE BUDGET (REPRINTED IN SENATE HEARINGS BEFORE THE COMMITTEE ON GOVERNMENT OPERATIONS ON BILLS RELATING TO PAYMENTS OF TAXES, OR IN LIEU OF TAXES, TO STATE OR LOCAL TAXING UNITS (PART 2), 84th Cong., 2d Sess. at 248-249 (1956))

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and to pledge the credit of the Government therefor, were limited to some cost-plus-a-fixed-fee construction contracts of the Navy. Report was also made of the fact that neither the Army nor the Air Force used the device and that the Navy made no use of it in any other type of contract, including firm fixed-price construction contracts.

We also indicated that whether use of the purchase-agent device would be extended or continued was being studied by a committee composed of representatives of the military departments as well as the Office of Secretary of Defense. In accordance with our commitment to provide you with the results of that study, we wish to advise that this study has now been completed. It has been determined that it will be the policy of the Department of Defense not to designate prime contractors on cross-type [sic] contracts to be performed within the continental limits of the United States, as agents of the Government for the purchase of supplies.

Sincerely yours,

R. C. LAMPHIER, JR., [sic]
Deputy Assistant Secretary of Defense
(Supply and Logistics).

ATOMIC ENERGY COMMISSION,
Washington, D.C., March 5, 1956

HON. JOHN L. MCCLELLAN,
Chairman, Committee on Government Operations,
United States Senate.

DEAR SENATOR MCCLELLAN: You have requested the comments of this Commission on S. 2100. That bill would prohibit any agency of the United States from entering into any contract by which a private person is constituted an agent of the United States for the purpose of purchasing or acquiring property necessary to carry out his contract, and with authority to purchase or acquire such property in the name of the United States or agency thereof. It would further render null and void, insofar as the application of State and local use taxes are concerned, any contract provisions constituting such a person an agent to purchase or acquire property.

The bill would appear to have two objectives: (1) To permit imposition of State and local sales and use taxes on purchases made by the United States through agents and (2) to prohibit the use by the United States for any purpose of contracts constituting the contractor a purchasing agent.

To the extent that the bill deals with a problem of State and local taxation, we believe it is a departure from sound principle. In *Alabama* v. *King and Boozer* (314 U.S. 1), the Supreme Court adopted the principle that a State may not constitutionally levy a sales or use tax on purchases made by the United States Government, whether or not such purchases are made through a contractor. It declared the question in such cases to be whether the United States was the purchaser; if it was, the transaction was tax-exempt, while if the contractor was the purchaser, the transaction was taxable. Finding in that case that the contractors made the purchases with their own funds and on their own credit, and did not have "the status of agents of the Government to enter into contracts or to pledge its credit" (314 U.S. at 13), it held the United States was not the purchaser and

the transaction could be taxed. In *Kern-Limerick, Inc.* v. *Scurlock* (347 U.S. 110), the Court, on a different set of facts, concluded that the United States was the purchaser, since the contractor executed the purchase documents on behalf of and as agent for the United States. In short, the Court held that the United States, like any private person, could act through an agent and that when it did so it was, as principal and under accepted doctrines of agency, the real party to the purchase transaction. The result is consistent with numerous decisions which have held in appropriate circumstances that a tax may be deemed imposed on the United States even though formally assessed against a private party (e.g., *United States* v. *Alleghany County*, 322 U.S. 174. 186-189, and cases cited; cf. *Mayo* v. *United States*, 319 U.S. 441).

Accordingly, we do not perceive a sound basis for distinguishing, for tax purposes, between purchases made by the United States directly and through contractors acting as agents.

S. 2100 as drafted, however, would do more than consent to the taxation of certain governmental purchases which are now tax exempt. Section 2 would declare purchase agency provisions "void" for certain purposes and section 1 would prohibit the entering into such provisions for any purpose. The effect would be to deny to the United States and its agencies, notwithstanding the provisions of any other act, the authority to enter into contracts constituting a private person a purchasing agent. Such a prohibition would significantly affect the operations of this Commission.

The authority of the Commission to constitute contractors its agents is supported by *Kern-Limerick Co.* v. *Scurlock*, *supra*, and by *DuPont* v. *Washington* (267 P. 2d 677).

The Commission's practice has been to conduct its operations to the maximum degree possible through contractors, thereby availing itself of industrial experience and ability, keeping to a minimum the size of the Commission's staff, and promoting ultimate industrial participation in the atomic energy industry. In general, it

has not entered into contracts expressly designating the contractor an agent. In some situations, however, it has found that particular functions can most effectively be carried out by contracts of express agency. These include the following:

(1) In the area of community management several contractors have been expressly designated agents to lease and manage Government-owned real property, and to operate Government-owned transportation systems, public utility systems, and hospitals on behalf of the Commission. In each of these cases, since the contractor is an agent for all other purposes, it would appear inappropriate to give it a different status for purposes of procurement of property needed for the contract work.

(2) Pursuant to the Federal Property and Administrative Services Act, many basic commodities needed by the Commission and its contractors for the carrying out of programs authorized by the Atomic Energy Act are procured through General Supply Schedule Contracts entered into by the General Services Administration for the benefit and use of other agencies of the United States. For purposes of administration, it has been found most efficient to authorize the Commission's cost-type management contractors to place orders against such contracts as agents for the Commission, rather than have the Commission place such orders. This arrangement has been acceptable to the General Services Administration and has worked effectively to expedite the contractors' operations on behalf of the Commission and to minimize the number of Commission personnel required. In these cases, although the contractor may not be expressly designated an agent for other purposes, it is necessarily an agent for the purpose of exercising rights under contracts entered into in the name of the United States, and is so designated.

(3) In a number of other situations the Commission has found it convenient to appoint cost-type management contractors its agents for the purpose of administering many substantial procurement contracts which were

placed directly by the Commission. In such cases the contractor so designated may perform many of the purchasing functions, such as receiving, inspecting, accepting or rejecting, and paying for the purchased materials on behalf of the Commission. While we do not believe such a relationship would come within S. 2100, the broad language of the bill as presently drafted might create doubts.

In addition to these situations, the bill might also create doubts with respect to a very large volume of purchases conducted by Commission cost-type contractors. Most of the Commission's major cost-type contracts may properly be described as management contracts under which the contractor is retained to construct or operate for the Commission facilities which the Commission owns. Typically, in such cases the contractor uses no funds of its own but is authorized to make payments out of Government funds which are advanced to it and held in a special Government contract account for the purpose. Typically, also, the contract provides that title to all goods purchased passes directly from the vendor to the United States—a provision which, among other things, renders theft or mutilation of such materials a Federal offense, facilitates transfer of them between Commission contractors as needed, and eliminates possible problems as regards claims or liens against such property stemming from other activities of the contractor not related to AEC work. In such cases, while the contractor is not expressly designated an agent, it is given authority to purchase or acquire property in the name of the United States, and to expend funds of the United States for that purpose. Consequently, there might be some question, should S. 2100 be enacted, whether this form of contracting would continue to be permissible.

Each of the forms of contracting described above has been adopted by the Commission because it was found to have significant practical advantages wholly apart from any tax consequences that might ensue. In particular, the Commission's method of contracting has facilitated the administration of a vast procurement effort, generally conducted under very tight time schedules, with a mini-

mum of Government personnel, while yet retaining basic financial and accounting checks necessary to safeguard the public interest. Adoption of S. 2100 might impose limitations on the Commission's contracting power, not based on any study of the particular situations which led to the adoption of particular contracting procedures, which would operate to the disadvantage of the Commission's program.

For the foregoing reasons we would not recommend enactment of S. 2100.

The Bureau of the Budget has advised that it has not objection to the transmittal of this report.

Sincerely yours,

K. E. FIELDS, *General Manager.*

ATOMIC ENERGY COMMISSION,
Washington, D.C., April 18, 1956.

HON. JOHN L. MCCLELLAN,
Chairman, Committee on Government Operations,
United States Senate.

DEAR SENATOR MCCLELLAN: This is in response to your requests for comment on bills S. 826, S. 1566, S. 1657, S. 2390, and S. 2754 of the 84th Congress, which would variously authorize taxation of certain Federal property by State and local tax authorities, and provide for payment by Federal agencies of sums in lieu of taxes with respect to certain other Federal property.

We have been informed by Senator Humphrey, of your committee, of the preliminary hearing on these bills which was held July 25, 1955, and of a contemplated further hearing in April, at which he will preside. The Commission believes that this letter will adequately express its views on the proposed legislation and has no desire to be heard orally.

THE BILLS

As a preliminary matter, comment by the Commission on S. 826 would not appear to be necessary because of its specific exemption for AEC property. S. 826 would per-

mit State and local taxation of, or payments in lieu of taxes on, defense production facilities. By definition, in section 3(c) of S. 826, a defense production facility would not include property owned or used by the AEC for purposes of the Atomic Energy Act of 1946, as amended. The reference to the 1946 act, as amended, would embrace the current Atomic Energy Act of 1954.

S. 1566, S. 1657, and S. 2390 open with the premise and declaration that the Federal Government is under no constitutional obligation to pay taxes or make contributions in lieu of taxes on account of Federal property. S. 1566 would declare it the policy of the United States to avoid, insofar as feasible, impairment of State and local finances through Federal acquisition of real or certain tangible personal property or Federal requirements for State and local services arising directly from Federal ownership or use of property. S. 1657 and S. 2390 would, in somewhat similar vein, declare it to be the policy of the United States to make fair and equitable tax payments and contributions in lieu of taxes to compensate the taxing authorities for tax revenue of which they are deprived by Federal ownership or control of property. All three bills state the purpose to avoid inequities between State and local taxpayers and Federal taxpayers in the distribution of tax burdens and governmental costs associated with Federal ownership or use of property. It is further stated that the State and local governments would be expected when requested, to make available to the Federal property, and residents thereon, the public services accorded other properties and residents upon the same terms.

In furtherance of these declarations and policies, the 3 bills set forth 2 broad groupings of provisions providing:

First, consent to State and local ad valorem taxes on certain classes of properties, principally property to which the Federal Government holds title to protect its financial interest in connection with loans or contracts of insurance or guaranty, or property to which it holds title but leases its interest or sells it conditionally to taxable persons; and

* * * * *

JOHN F. McNETT AFFIDAVIT 10/5/77, FILED IN SUPPORT OF PLAINTIFF'S OPPOSITION TO DEFENDANTS' CROSS-MOTION FOR SUMMARY JUDGMENT w/EXHIBITS A-E (R.III)

IN THE UNITED STATES DISTRICT COURT FOR THE DISTRICT OF NEW MEXICO

Civil Action No. 74-418M

UNITED STATES OF AMERICA, PLAINTIFF

vs.

STATE OF NEW MEXICO; BUREAU OF REVENUE OF THE STATE OF NEW MEXICO; and FRED L. O'CHESKEY, as Commissioner of Revenue of and for the State of New Mexico, and his successors in office, DEFENDANTS

AFFIDAVIT

I, JOHN F. McNETT, being first duy sworn, state:

1. I am Assistant Chief Counsel, United States Department of Energy (DOE), formerly the Energy Research and Development Administration (ERDA), Albuquerque Operations Office, Albuquerque, New Mexico, and as such I am the staff attorney in DOE responsible for coordinating the above-entitled civil action with our DOE Washington Headquarters Office and with the Tax Division of the United States Department of Justice, the agency with the responsibility for handling the above-entitled litigation. In an affidavit submitted in the above-entitled action in support of plaintiff's motion for summary judgment filed March 29, 1976, I stated the background and events following the cited decision of the New Mexico Court of Appeals.

2. The case referred to in paragraph 1. was decided on a stipulation which was submitted as Exhibit 1 to my earlier affidavit. Attached as exhibits to that stipulation in the record before the New Mexico Court of Appeals were eight documents, listed in paragraph 13. of the stipulation, by various officials and employees of the State of New Mexico between 1947 and 1961. These documents

were the ones to which the New Mexico Court of Appeals referred in its opinion at 531 P.2d at 213-214.

3. Attached hereto as Exhibits 2-A through 2-E to this affidavit are five of the eight documents referred to in paragraph 2. as follows:

A. Letter, Commissioner Lujan to AEC, December 29, 1950.

B. Letter, Assistant Attorney General McCulloch to Bureau of Revenue, School Tax Division, January 7, 1954.

C. Letter, Bureau of Revenue (Barker) to AEC, July 2, 1957.

D. Letter, Bureau of Revenue (Robinson) to AEC, August 28, 1959.

E. Letter, Bureau of Revenue (Lujan) to AEC, November 8, 1949.

4. On May 3, 1977, I attended the deposition of Daniel H. McGrath, Jr.; Acting Director, Special Financing Staff, Bureau of Government Financial Operations, U.S. Department of Treasury. Prior to his deposition, Mr. McGrath furnished to counsel for defendants and counsel for plaintiff statistical data concerning the use of the letter-of-credit method of financing. Attached hereto as Exhibit F is a document entitled "Numbers and Amounts of Letters-of-Credit-FRB System for Period Ending March 8, 1977," which was prepared by the Special Financing staff on the basis of U.S. Treasury Department records and furnished to counsel, along with other statistical data, prior to the McGrath deposition.

/s/ John F. McNett
JOHN F. MCNETT

SUBSCRIBED AND SWORN TO before me this 5th day of October, 1977.

/s/ Elizabeth R. Gallegos
Notary Public

My Commission Expires February 27, 1981.

EXHIBIT 2-A

Re: C-2

Mr. Chalmers C. King
Acting Assistant General Counsel
United States Atomic Energy Commission
Santa Fe Operations Office
Los Alamos, New Mexico

Dear Mr. King:

I have made a careful study of your letter of December 28 concerning the change in status of the Zia Company with reference to their relationship with the Atomic Energy Commission. Without going into detail, it is my opinion bases upon the statements made in your letter and upon the exhibits attached thereto that the Zia Company is, so long as it is acting under those conditions, acting purely as an agent of the Atomic Energy Commission and that the purchases made are as such agent and not for themselves; that since the title to all property of whatever kind immediately vests in the Atomic Energy Commission when it passes from the supplier, therefor the payments are in fact being made by the suppliers directly to an agency of the United States government and are, therefor, within the cloak of the exemption provided for in Section 76-1405 of the New Mexico Statutes Annotated so that the suppliers need not include their receipts from such sales in their gross receipts when computing the School Tax due to the State of New Mexico.

Since the same condition exists with reference to purchases made outside of the State of New Mexico, it is, also, my opinion limited by the statements made and the exhibits furnished in your letter of December 28 that the New Mexico Compensating Tax would not attach as against the Zia Company.

Very truly yours,

LOUIS C. LUJAN
Commissioner of Revenue

December 29, 1950

EXHIBIT 2-B

STATE OF NEW MEXICO
Office of Attorney General

Santa Fe, New Mexico
January 7, 1954

J. C. Bergere, Director
School Tax Division
Bureau of Revenue
Santa Fe, New Mexico

Dear Mr. Bergere:

In your letter dated December 28, 1953, you submitted additional information concerning the activities of the Zia Company at Los Alamos for our information in connection with an opinion written to you relative to taxing the Zia Company on its operation of the Lodge at Los Alamos.

After studying this additional information and seeing the contract which the Zia Company has with the Atomic Energy Commission, it is apparent that the Zia Company acts more in the nature of an agent than of an independent contractor and that the items purchased by it are actually purchased with government funds and title vests in the government immediately.

For these reasons, you may consider Opinion No. 5845 to the effect that the Zia Company is liable for gross receipts tax on its operations in Los Alamos, particularly at the Lodge, as being overruled and withdrawn.

Very truly yours,

/s/ C. C. McCulloh
Assistant Attorney General

EXHIBIT 2-C

July 2, 1957

Mr. Sterling F. Black, Counsel
Atomic Energy Commission
Los Alamos, New Mexico

YOUR REFERENCE: LC:JC

Dear Mr. Black:

I am in receipt of your letter of June 28th with which you transmitted excerpts from the contracts between the Atomic Energy Commission and the Zia Company and the ACF Industries, Inc.

With respect to the Zia Company contract, I note under Article XIII, Paragraph C, that except as otherwise directed by the Commission, title to all property of every kind and description acquired by the Contractor, the cost of which is allowable under this contract, (covered by other provisions of the contract), shall pass directly from the vendor to the Government, and in view of this provision, I am of the opinion that no property purchased and paid for with Government funds, as provided in the contract, would be subject either to the sales tax or compensating tax.

As I have advised you before, I don't consider the privilege tax upon the Zia Company as contractor as enforceable, since the contract is made directly with a government agency.

With regard to the ACF Industries, Inc. contract, I find substantially the same provisions contained in Article XI, Paragraph 3 with respect to title to property acquired and used in the performance of the contract as found in the Zia Company contract, and my opinion as to the taxability upon the purchase and use of the property and upon the contractor for the privilege of doing business is the same as hereinbefore mentioned as to the Zia Company contract.

As heretofore stated to you and your associates, I am definitely of the opinion that there is no tax liability arising in any respect upon the contract with the University of California or the contract with the Sandia Corporation, both of which are non-profit organizations.

Your very truly,

CHARLES B. BARKER
Attorney
Bureau of Revenue

CBB/gt

cc: School & Compensating Tax Division

EXHIBIT 2-D

STATE OF NEW MEXICO
BUREAU OF REVENUE
Legal Division
Santa Fe

[SEAL]

August 28, 1959

Mr. Chalmers C. King
U. S. Atomic Energy Comm.
P. O. Box 5400
Albuquerque, New Mexico

Dear Mr. King:

I am in receipt of your letter regarding the purchases of gasoline by ACF Industries Inc., from the Texaco Co., wherein you state that the Texaco Co., informed ACF the following: "It is our understanding that New Mexico's Senate Bill No. 120 applies only to direct agencies of the Federal Government and it is also our understanding that Mr. Johnny Walker, Director of the New Mexico Bureau of Revenue has ruled that ACF is not exempt from this tax."

You further state in your letter that it is your position, "that the purchase of tangible personal property by a cost-type, advanced funds contractor of the United States Atomic Energy Commission, such as ACF, is tantamount to a purchase of the property by the Commission itself has been consistently recognized in the administration of the Emergency School Tax Act."

This is to inform you that the Bureau of Revenue of the State of New Mexico has taken a position that sales to the cost-type advanced fund contractors who are by federal law agents of the Federal Government are exempt from the Emergency School Tax Act under the provi-

sions of Senate Bill No. 120. At the present time we recognize three of such industries within the State of New Mexico, ACF Industries Inc., Zia Co. and the Sandia Corp. I am enclosing a copy of a letter this office prepared to Mr. John C. Burke, operating manager of the General Electric Supply Co., which may be of some assistance to you.

We hope this sufficiently answers your question but if we may be of further service please let me know.

Sincerely yours,

/s/ Richard H. Robinson
RICHARD H. ROBINSON
Chief Counsel
Bureau of Revenue

RHR/ls

EXHIBIT 2-E

COPY

NEW MEXICO
BUREAU OF REVENUE
SANTA FE, NEW MEXICO

November 8, 1949

United States Atomic Energy Commission
Santa Fe Operations Office
Los Alamos, New Mexico

Attention Mr. Chester G. Brinck

Dear Mr. Brinck:

I have made a careful study of your letter of November 1st, together with enclosure attached thereto, and in reply to that letter I should like to split my opinion; one part of the opinion being directed to the position of the Sandia Corporation under the New Mexico Emergency School Tax Act and the other part of the opinion being directed to their position under the New Mexico Compensating Tax Act.

After a careful consideration of the material which you sent me, which includes a copy of the contract between the Atomic Energy Commission and Western Electric Company, Inc.; a copy of Sandia Corporation's letters of October 28, 1949 to the First National Bank in Albuquerque and to the Albuquerque National Bank at Albuquerque, and a copy of letter of October 31st from the Atomic Energy Commission to George A. Landry, President of the Sandia Corporation, at Albuquerque, New Mexico, I have come to the conclusion that title to all property of whatever kind acquired by the Sandia Corporation will pass directly from vendors to the Atomic Energy Commission, that the Sandia Corporation will pay for such property with money belonging to the Atomic Energy Commission, even though on deposit to the memo of Sandia Corporation.

It is therefore my opinion that the gross receipts from sales made in New Mexico are not to be included by vendors in their gross receipts for tax purposes, since such receipts are exempted under the provisions of Section 76-1405 New Mexico Statutes, 1941, Annotated.

Since title to all property purchased outside of the State of New Mexico rests immediately in the Atomic Energy Commission, without passing through Sandia Corporation, it is my opinion that the storage, use or other disposal of such properties is exempted under the provisions of Section 76-1504, New Mexico Statutes, 1941 Annotated.

Very truly yours,

/s/ Louis C. Lujan
LOUIS C. LUJAN
Attorney
Bureau of Revenue

LCL:cp

EXHIBIT 1 TO AFFIDAVIT OF JOHN F. McNETT FILED IN SUPPORT OF PLAINTIFF'S OPPOSITION TO DEFENDANTS' OTHER PROCEDURAL DEFENSES

BEFORE THE COMMISSIONER OF REVENUE STATE OF NEW MEXICO

IN THE MATTER OF THE PROTEST OF THE ZIA COMPANY AND THE UNITED STATES OF AMERICA AGAINST ASSESSMENT NO. 109339

IN THE MATTER OF THE PROTEST OF LOS ALAMOS CONSTRUCTORS, INC., AND THE UNITED STATES OF AMERICA AGAINST ASSESSMENT NO. 109341

STIPULATION

The United States of America, hereinafter called "U.S.," The Zia Company, hereinafter called "Zia," Los Alamos Constructors, Inc., hereinafter called "LACI," and the Bureau of Revenue of the State of New Mexico, acting with the Attorney General of the State of New Mexico, hereinafter called "Bureau," hereby stipulate and agree that the facts contained in this stipulation are to be deemed received in evidence in all further proceedings, including actions in any court, and are to be treated as having been conclusively established by competent evidence.

* * * * *

4. For purposes of this stipulation, all tangible personal property needed for the performance of Contract ENG-90, has been purchased from non-government sellers, some of whom were transacting or engaging in business in New Mexico, others of whom were not transacting or engaging in business in New Mexico. All such property has been purchased by the issuance of purchase orders by and in the name of Zia. All such purchases have been conducted in accordance with Article X, "Subcontracts, Purchase Orders and Procurement," of Con-

tract ENG-90 and in accordance with the provisions of Article XIV, "Property," of Contract ENG-90. The contracting officer of Contract ENG-90, in accordance with the second sentence of paragraph 2 of Article XIV, did not at any time provide otherwise than for passage of title to property directly from the vendor to the U.S. to the extent specified in the contract. Attached hereto as "Exhibit 3," comprising 2 pages, "Exhibit 4," comprising 2 pages, and "Exhibit 5," comprising 5 pages, are copies of purchase order forms used in procurement of tangible personal property by Zia during the period January 1, 1966, through June 30, 1967. "Exhibit 3" was used for all procurements between January 1, 1966, and approximately May of 1967. From May 1967 through June 1967, "Exhibit 4" was used for procurements under $2500 and "Exhibit 5" was used for procurements over $2500.

5. LACI, a corporation organized and existing under the laws of the State of New Mexico, has, since March 31, 1953, been performing work for AEC under a written contract, designated Contract AT(12-1)-1357, hereinafter called "Contract 1357." Through June 30, 1967, 38 written modifications to Contract 1357 had been executed by the parties. At all times, Contract 1357 provided, in general, that LACI would perform construction, alteration, and repair work, and other related work, for AEC in support of AEC research and development * * *

AFFIDAVIT OF JOHN F. McNETT, FILED IN SUPPORT OF PLAINTIFF'S OPPOSITION TO DEFENDANTS' OTHER PROCEDURAL DEFENSES W/EIGHT EXHIBITS (R.I. 43-81)

IN THE UNITED STATES DISTRICT COURT FOR THE DISTRICT OF NEW MEXICO

Civil Action No. 75-418

UNITED STATES OF AMERICA, PLAINTIFF

v.

STATE OF NEW MEXICO; BUREAU OF REVENUE OF THE STATE OF NEW MEXICO; and FRED L. O'CHESKEY, as Commissioner of Revenue of and for the State of New Mexico, and his successors in office, DEFENDANTS

AFFIDAVIT

JOHN F. McNETT, being first duly sworn, deposes and says:

1. I have since July 3, 1961, been employed as an attorney in the Office of Chief Counsel of the Albuquerque Operations Office (ALO) of ERDA, formerly AEC. Throughout my employment with AEC and ERDA I have had responsibility for handling state and local tax problems which arise in the conduct of ALO activity, including problems arising under the New Mexico Emergency School Tax Act, the New Mexico Compensating Tax Act, and the New Mexico Gross Receipts and Compensating Tax Act. I was the attorney primarily responsible for the handling of AEC's participation in discussions and litigation with the Bureau of Revenue, State of New Mexico, which ultimately resulted in the decision of the New Mexico Court of Appeals in *United States of America, Zia, and LACI* v. *Bureau of Revenue, State of New Mexico*, 87 N.M. 164, 531 P.2d 212 (1975).

2. In the summer of 1967 the Bureau of Revenue, State of New Mexico, with AEC consent audited the financial books and records of AEC pertaining to operations under AEC contracts with the Zia Company (Zia) and Los Alamos Constructors, Inc. (LACI) during the period July 1, 1964, through June 30, 1967. At the conclusion of this audit, on August 25, 1967, the Bureau of Revenue issued assessments under the Emergency School Tax Act and the Compensating Tax Act against Zia and LACI: (1) for school taxes (i.e., gross receipts taxes) upon and measured by AEC funds advanced for contract operations during the audit period and (2) for compensating taxes on the use of tangible personal property procured from private vendors in performance of the Zia and LACI contracts during the audit period. Zia, LACI, and the United States Government (acting through the Department of Justice at the request of AEC) filed protests against these assessments with the Commissioner of Revenue, State of New Mexico under the New Mexico Tax Administration Act. At no time throughout the proceedings and litigation which ensued did the Commissioner of Revenue or any of his attorneys question the right of the United States to be a party to any of the proceedings.

3. Upon issuance of assessments and filing of protests referred to in paragraph 2, there followed a series of meetings and discussions, extending over a period of several years, between and among officials of Zia, LACI, and AEC, the Commissioner of Revenue, their attorneys, and attorneys of the U.S. Department of Justice concerning the assessments, the issues raised by them, and possible methods of resolution. In 1969 these discussions finally resulted in an agreement among all concerned, including then Commissioner of Revenue Franklin Jones, that issues then unresolved would be submitted to the New Mexico Court of Appeals for resolution on a stipulated statement of facts with exhibits. Attached hereto as Exhibit 1 is the stipulation, without exhibits, on which the issues

raised by the 1967 assessment against Zia and LACI were submitted to the New Mexico Court of Appeals.

4. One issue raised in the test litigation referred to above was whether purchases of tangible personal property for AEC accomplished by the issuance of purchase orders by Zia and Sandia Corporation qualified for a deduction under the New Mexico Gross Receipts and Compensating Tax Act for sales to the United States. To protect the interests of vendors, the Bureau of Revenue and AEC on this issue during the period of the litigation, the Bureau and AEC entered into an agreement, designated Contract AT(29-2)-2849 (Contract 2349). Under Contract 2849 Zia and Sandia Corporation were permitted to issue special nontaxable transaction certificates to their vendors of tangible personal property while the issue of the tax treatment of these transactions was being litigated. AEC agreed that payment would be made to the Bureau for these taxes if test litigation held that such taxes were owing. A copy of Contract 2849 is attached hereto as Exhibit 2. The Commissioner of Revenue authorized the special nontaxable transaction certificates provided for in Contract 2849 in Ruling 69-001-18 of the Commissioner of Revenue, dated December 18, 1969. A copy of Ruling 69-001-18 is attached hereto as Exhibit 3.

5. On January 8, 1975, the New Mexico Court of Appeals handed down its decision reversing the Commissioner of Revenue on the Zia and LACI protests against the assessments referred to in paragraph 2. The decision is reported in 87 N.M. 164, 531 P.2d 212 (1975).

6. The Commissioner of Revenue did not seek further review of the decision of the New Mexico Court of Appeals referred to in paragraph 5. I prepared for the signature of the Manager, ALO, a letter to the Commissioner of Revenue dated January 30, 1975, requesting that permanent nontaxable transaction certificates be issued to replace the temporary ones authorized by Ruling 69-001-18, that the Commissioner agree that the rec-

ord keeping required by ERDA by Contract 2849 is no longer necessary, and that the principles enunciated in the concurring opinion of Judge B. C. Hernandez be recognized by the Commissioner of Revenue. A copy of the January 30, 1975, letter from the Manager, ALO, to the Commissioner of Revenue is attached hereto as Exhibit 4. The Commissioner of Revenue responded to Exhibit 4 in a letter dated February 28, 1975, by denying all of the requests made in Exhibit 4. The Commissioner's letter of February 28, 1975, is attached as Exhibit 5.

7. As of June 30, 1975, Zia and Sandia Corporation had reported total estimated contingent liabilities of ERDA under Contract AT(29-2)-2849 in an estimated amount of $8,939,000. In addition, erroneous application of the 4% New Mexico gross receipts tax to ERDA advanced funds would subject ERDA to liabilities estimated at $10,000,000 per year.

8. At some point after the litigation referred to in preceding paragraphs was submitted to the New Mexico Court of Appeals, attorneys for the New Mexico Bureau of Revenue began taking the position, contrary to that taken in the test litigation, that the United States could not be a party to Tax Administration Act proceedings before the Commissioner of Revenue in which contractors of the United States were being assessed taxes. The Bureau took this position even when it was apparent that the United States would ultimately be required to pay the taxes assessed and when the United States claimed that the purported taxes were erroneous and in violation of its sovereign rights. I first became aware of this reversal of the Bureau's position in connection with a protest filed by Ross Aviation, Inc., an AEC, ALO contractor. At the request of AEC, attorneys for the Department of Justice moved to intervene in the proceedings before the Commissioner of Revenue on protests previously filed by Ross Aviation. The Commissioner of Revenue's delegate conducted a hearing on the Government's motion to inter-

vene on April 3, 1974, and denied the Government's motion in a ruling dated April 11, 1974. A copy of the Bureau of Revenue ruling of April 11, 1974, is attached hereto as Exhibit 6.

9. ERDA responded to the Commissioner's letter of February 28, 1975, Exhibit 4, with a letter of March 12, 1975, a copy of which is attached hereto as Exhibit 7. In Exhibit 7 a meeting between ERDA and Bureau representatives was proposed, and ERDA requested that Contract 2849 be amended to include another ERDA advanced fund contractor, Wallace/Brown-Olds/Howard, among those contractors authorized to issue special nontaxable transaction certificates pending final resolution of the issues of tax liability.

10. The Commissioner responded to ERDA's letter of March 12, 1975. Exhibit 7, with a letter of May 16, 1975, a copy of which is attached hereto as Exhibit 8. In Exhibit 8 the Commissioner agreed to meet with ERDA representatives, denied the ERDA request to authorize Wallace/Brown-Olds/Howard to issue special nontaxable transaction certificates under Contract 2849, and stated his preference for conducting audits of contractors performing work for the Government in order to resolve issues left unsettled in the *Zia* decision.

11. On July 17, 1975, I attended a meeting with Commissioner O'Cheskey, his attorneys, and Mr. Charles E. Stratton of the U.S. Department of Justice. At the July 17, 1975, meeting Commissioner O'Cheskey and his attorneys reiterated their positions that the concurring opinion of Judge Hernandez in the *Zia* case was incorrect and not binding on the Bureau and that the United States was not a proper party to proceedings before the Commissioner of Revenue in which tax liabilities of its contractors were at issue. Mr. Stratton advised Mr. O'Cheskey of the Government's intent to file the present suit for declaratory relief in the Federal District Court for the District of New Mexico.

12. As of this date the Bureau has not authorized Wallace/Brown-Olds/Howard to issue special nontaxable transaction certificates under Contract 2849, nor authorized the use of permanent nontaxable transaction certificates by any ERDA contractor. The use of permanent nontaxable transaction certificates applicable to sales of tangible personal property to the United States would relieve ERDA and its contractors of the record-keeping requirements of Contract 2849.

/s/ John F. McNett
JOHN F. MCNETT

SUBSCRIBED AND SWORN TO before me this 16th day of January, 1976.

/s/ Elizabeth R. Gallegos
Notary Public

My commission expires February 27, 1977.

SUPREME COURT OF THE UNITED STATES

No. 80-702

UNITED STATES, PETITIONER

v.

NEW MEXICO, ET AL.

ORDER ALLOWING CERTIORARI

Filed February 23, 1981

The petition herein for a writ of certiorari to the United States Court of Appeals for the Tenth Circuit is granted.

Justice Stewart took no part in the consideration or decision of this petition.

U. S. GOVERNMENT PRINTING OFFICE: 1981 351789 879

Supreme Court, U. S.
FILED
JAN 5 1981
MICHAEL RODAK, JR., CLE

No. 80-702

IN THE

Supreme Court of the United States

October Term, 1980

UNITED STATES OF AMERICA, PETITIONER

v.

STATE OF NEW MEXICO, ET AL., RESPONDENTS

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE TENTH CIRCUIT

BRIEF FOR RESPONDENTS IN OPPOSITION

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IN THE

Supreme Court of the United States

October Term, 1980

No. 80-702

UNITED STATES OF AMERICA, PETITIONER

v.

STATE OF NEW MEXICO, ET AL., RESPONDENTS

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE TENTH CIRCUIT

BRIEF FOR RESPONDENTS IN OPPOSITION

The Attorney General of the State of New Mexico submits his brief in opposition to the petition of the United States of America for a writ of certiorari to review the judgment of the United States Court of Appeals for the Tenth Circuit in this case.

OPINIONS BELOW

The opinion of the district court (App. A of Petition) is reported at 455 F. Supp. 993. The opinion of the court of appeals (App. B of Petition) is reported at 624 F.2d 111.

JURISDICTION

The jurisdictional requisites are adequately set forth in the Petition, except that the time for New Mexico to file its Brief in Opposition was extended to January 6, 1981 by letter from the Clerk of November 25, 1980.

STATUTES INVOLVED

The pertinent parts of New Mexico's Gross Receipts and Compensating Tax Act are set forth in Appendix D of the Petition. The sections as designated in the Appendix, and the current designation in the 1978 compilation, are:

Appendix		1978 Compilation
§§ 72-16A-3	–	§§ 7-9-3
72-16A-4	–	7-9-4
72-16A-7	–	7-9-7
72-16A-12	–	7-9-12
§§ 72-16A-12.1	–	§§ 7-9-13
72-16A-12.2	–	7-9-14
72-16A-14	–	7-9-45
72-16A-14.9	–	7-9-54

41 U.S.C. § 255, 31 C.F.R. Part 205 (1979), and § 4(c) (2) of the Atomic Energy Act of 1946, 60 Stat. 755, are reproduced as Appendices A, B, and C, respectively, attached to this brief.

QUESTIONS PRESENTED

1. Whether three private corporate contractors performing contracts for the United States Department of Energy ("DOE"), successor to the Energy Research and Development Administration ("ERDA"), are exempt from the New Mexico gross receipts and compensating taxes (§§ 7-9-1 through 7-9-81, NMSA 1978) on the funds utilized by them to pay salaries, operating costs, award fees and third-party suppliers.

2. Whether reliance by three private corporate contractors on an "advanced funding" arrangement pursuant to 41 U.S.C. § 255, § 4(c) (2) of the Atomic Energy Act of 1946, 60 Stat. 755, now codified at 42 U.S.C. § 2061(b), and 31 C.F.R. Part 205 (1979) to finance their performance of contract work for the Department of Energy renders such contractors federal agents exempt from the New Mexico gross receipts tax on such funds.

3. Whether, in the absence of congressional authorization, Department of Energy contracting officers may insert agency-creating clauses in contracts with three private corporate contractors to insulate them from the New Mexico gross receipts and compensating taxes.

STATEMENT OF THE CASE

1. The United States instituted the present declaratory judgment action in 1975 to determine the liability for the New Mexico gross receipts and compensating taxes* of three private corporate contractors working for the Atomic Energy Commission ("AEC"), whose responsibilities were first shifted to the Energy Research and Development Administration ("ERDA"), and then to the Department of Energy ("DOE").** A companion case, holding Army contractors liable for these same taxes, was not appealed beyond the Tenth Circuit, *United States v. New Mexico*, 581 F.2d 803 (10th Cir. 1978). While New Mexico had viewed AEC contractors as exempt from the Emergency School Tax Act, predecessor to the gross receipts tax, it reversed its position in 1967 when the Gross Receipts and Compensating Tax Act was enacted, placing the United States on notice from then on. See *United States v. Bureau of Revenue*, 87 N.M. 164, 531 P.2d 212 (Ct. App. 1975) (Petition, App. B, 12a, n.3).

Atomic Energy Commission contractors as a class were once immune from state taxes, *Carson v. Roane-Anderson Company*, 342 U.S. 232 (1952), an immunity subsequently withdrawn by Congress through amendment of the Atomic Energy Act to place them on the same footing as contractors of other agencies. Act of August 13, 1953, 67 Stat. 575 (Petition, App. B, 15a, 21a).

The New Mexico gross receipts tax is levied on gross receipts from selling property or performing services within the state (Petition, App. D, 31a). The compensating tax is levied on the value of property imported into the state, complementing the gross receipts tax on in-state transactions (Petition, App. D, 32a).

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* Sections 72-16A-1 through 72-16A-19 (Supp. 1975); now codified as §§ 7-9-1 through 7-9-81, NMSA 1978.

** All three abbreviations are used interchangably herein, depending on the context.

The imposition of the gross receipts tax, as its name suggests, is not dependent on a taxpayer showing a profit (Petition, App. B, 18a, n.6).

The New Mexico taxes are routinely levied on the receipts of federal contractors, *United States v. New Mexico*, 581 F.2d 803 (10th Cir. 1978). For analytical purposes, these receipts may be divided into three categories: the salaries of contractor personnel and internal operating expenses, the cost of supplies purchased from third parties and, where applicable, a contractor's stipulated fee (Petition, App. B, 24a, n.11). A vendor of supplies to a contractor is also potentially subject to tax on his receipts, although non-taxable transaction certificates are provided for many such transactions to avoid pyramiding of tax, § 7-9-47, NMSA 1978 (Supp. 1980).

The United States' sole contention is that the three DOE contractors are federal agents in disbursing funds to their employees and suppliers and fee payments to themselves (Petition, App. B, 12a). It is asserted that the funds utilized by the contractors are therefore exempt from the New Mexico taxes either because the funds belong to the contractors' principal, the United States, or because the legal incidence of the New Mexico taxes would impermissibly fall on the United States through its agents. Similarly, vendors of supplies to the agent-contractors would also be entitled to a deduction on their receipts, § 7-9-54, NMSA 1978 (Supp. 1980).

If the contractors are not agents, they would be liable for gross receipts tax on the funds they receive to cover salaries and operating costs, purchased supplies and their own fees. Their liability for the compensating tax would also follow (Petition, App. B, 11a, n.1).

2. The three contractors are Sandia Corporation, a subsidiary of Western Electric Company, Inc.; the Zia Company, a subsidiary of Santa Fe Industries, Inc.; and Los Alamos Constructors, Inc. (LACI), a subsidiary of the Zia Company. Their tasks and

property ownership are adequately set forth in the Petition at page 2, with the addition that Zia and LACI concede their liability for gross receipts tax on their fixed fees (Petition, App. B, 24a, n.11).

The three contractors operate under "standard Atomic Energy Commission (now DOE) management contracts" (Petition, 2). Thus, the three contractors perform their work at a federal facility, require approval by the United States of purchases above specified amounts, are subject to general supervision by United States personnel, furnish virtually none of their own property, cause title to their purchases to pass from the vendor directly to the United States and are essentially protected from loss in contract performance since all their costs are compensated by the United States (Petition, App. B, 14a, 19a-21a, 25a, n.12).

Like many ERDA contractors, the three contractors are financed through an "advanced funding" arrangement which relieves them of the need to borrow capital (Petition, App. B, 24a). This arrangement is adequately described in the Petition at page 3 with the additions that advanced funding is prescribed for general use in government contracting in 41 U.S.C. § 255 and 31 C.F.R. Part 205 (1979) and for AEC contractors specifically in § 4(c) (2) of the Atomic Energy Act of 1946, see Appendices A, B, and C, attached to this brief. Also, the contractors draw on advanced funds, among other things, to make salary payments to their employees and fee payments to themselves (Petition, App. B, 21a).

The United States concedes that the privately-owned contractors are not federal instrumentalities* (Petition, App. B, 21a). The United States concedes that the contractors are not federal agents in "directing the details of day-to-day research or

* The Atomic Energy Act defines "Government agency" as an "independent establishment" or "corporation" which is "wholly or partly owned by the United States of America" and which is also "an instrumentality of the United States. . .", 42 U.S.C. § 2014(1) (Petition, App. B, 21a).

maintenance and the hiring and direct supervision of employees" (Petition, App. B, 18a, n.6). The United States concedes that the contractors' employees are not employees of the United States, that the contractors' employees may make no claims directly against the United States, and that the United States is not liable for contractor torts (Petition, App. B, 18a, n.6).

The contractors are required to make purchases and subcontracts in their own names. Their purchase forms clearly distinguish between the "Buyer" – Sandia, Zia or LACI – and the "Government" (Petition, App. B, 26a, n.6).

More than 8,000 contractors with other agencies are financed through "advanced funding", as contrasted with only 165 within ERDA (Petition, App. B, 24a, n.10). No claim of agency relationship could seriously be made for many of the non-ERDA recipients even though they are financed exactly as are the ERDA contractors (Petition, App. B, 23a). Even within ERDA, advanced funding was adopted as simply another means of reimbursing contractors and eliminating weaknesses in the government's bookkeeping practices (Petition, App. B, 23a, 24a).

Sandia receives no fee under its ERDA contract. However, its profit-conscious parent company receives royalty-free licenses on communication-related patents developed by Sandia. The United States pays Sandia's overhead and the salaries of parent-company employees used in the course of Sandia operations. Sandia's parent is also paid by the United States for furnishing a variety of auditing, research and supervisory services. ERDA regulations concerning fee determinations do not evidence any intent to create an agency relationship by omitting a fee (Petition, 24a, n.12; 25a).

Two years into this litigation, the local ERDA contracting officers in New Mexico modified the three contracts to refer directly to the three contractors as agents. The modifications contain the following caveat:

> This article shall not be construed to modify any other provisions of the contract . . . nor shall it create rights or obligations not otherwise provided for in the contract. (Petition, App. B, 26a).

3. On cross motions for summary judgment, the District Court found for the United States (Petition, App. A). Relying on *Livingston v. United States,* 179 F. Supp. 9 (E.D.S.C. 1959), *aff'd per curiam,* 364 U.S. 281 (1960), it held that the contracts and factual circumstances – most importantly the use of advanced funding – indicated an agency relationship (Petition, App. A, 4a, 6a). The advanced funding significantly distinguished these contractors from typical cost-plus contractors, and use of the funds did not constitute receipt of reimbursements for contractor expenses (Petition, App. A, 5a). If the contractors were agents in procuring supplies, they must also be agents in disbursing funds to their employees and themselves for salaries and operational costs (Petition, App. A, 9a).

On appeal, the Court of Appeals for the Tenth Circuit reversed (Petition, App. B). While recognizing that "a federal agency may bring a contractor within the scope of intergovernmental immunity . . ." (Petition, App. B, 17a), it declined to find that the use of advanced funding created an agency relationship. Since the "contractors are separate entities solely responsible for their own employees and internal management . . .", it follows that payments for salaries and overhead meet the contractors' "own obligations . . . regardless of the funding device employed" (Petition, App. B, 18a, 19a). The widespread use of advance funding to finance obvious non-agents outside ERDA (Petition, App. B, 23a, 24a), and the equally widespread use within ERDA, indicated that some additional "special arrangement" would be needed to create agency relationships (Petition, App. B, 21a).

The court relied on *United States v. Boyd,* 378 U.S. 39 (1964), because "all the same factors present here" were

advanced in that case in unsuccessfully claiming an agency relationship (Petition, App. B, 20a). While acknowledging that a use tax, rather than a sales tax, was at issue in *Boyd*, the court observed that "using government property in the course of performing a government contract is not unlike incurring obligations to achieve the same end" (Petition, App. B, 20a, n.7).

The court held that Sandia's no-fee arrangement did not bring it within the tax-exempt ambit of *Livingston v. United States*, 179 F. Supp. 9, (E.D.S.C. 1959), *aff'd per curiam*, 364 U.S. 281 (1960), because Sandia and its parent company derived demonstrable monetary and business benefits from contract performance, unlike du Pont in the earlier case (Petition, App. B, 25a, n.12).

The contract amendments adding carefully qualified agency language were discounted by the court because "By their terms, . . . the amendments add nothing substantive to the contracts . . ." (Petition, App. B, 25a). Since "the provisions of the contracts before the amendments did not establish agency status, we need not be swayed by amendments which make no changes" (Petition, App. B, 26a). Furthermore, the new language was not added to the contractors' purchase forms which continued to distinguish between the "Buyer" and the "Government" (Petition, App. B, 26a).

REASONS FOR DENYING THE PETITION

1. The United States alleges a conflict between the decision of the Tenth Circuit and *Kern-Limerick, Inc. v. Scurlock*, 347 U.S. 110 (1954); *Livingston v. United States*, 179 F. Supp. 9 (E.D.S.C. 1959), *aff'd per curiam*, 364 U.S. 281 (1960); *United States v. Boyd*, 211 Tenn. 139, 363 S.W. 2d 193 (1962), *aff'd*, 378 U.S. 39 (1964); and *United States v. Nevada Tax Commis-*

sion, 291 F. Supp. 530 (D. Nev. 1968), *aff'd*, 439 F.2d 435 (9th Cir. 1971) (Petition, 7).*

In fact, the present decision neither conflicts with the cited cases nor departs from the "uniform national rule" (Petition, 8) concerning state tax treatment of federal contractors. The decision of the Tenth Circuit reflects scrupulous adherence to the precedents of this Court and decisions of other courts of appeal. It properly applies them to the particular taxes at issue and the extensive factual development and numerous concessions in the present case.

In *James v. Dravo Contracting Company*, 302 U.S. 134 (1937) and *Alabama v. King & Boozer*, 314 U.S. 1 (1941), this Court established the general rule that federal contractors are subject to non-discriminatory state taxes. The fact that the economic burden of a tax might be passed on to the United States pursuant to contract would not bar its application.

The most obvious exception to this rule occurs where the legal incidence of a state tax falls on the United States. In recent years, the major concentration of this Court in adjusting federal-state relations in the area of tax has been to determine the legal incidence of particular states' taxes. See *United States v. County of Fresno*, 429 U.S. 452 (1977); *Diamond National Corporation v. State Board of Equalization*, 425 U.S. 268 (1976);

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* The cited decisions deal only with the imposition of sales taxes on *purchases* by federal contractors. To the extent the present decision applies the New Mexico gross receipts tax to funds utilized by the contractors to pay salaries and internal operating costs (some 58% of their expenditures), there is no conflict with the cited decisions since they did not address this issue in any way. As the Tenth Circuit observed, given the concession that the contractors' employees were their own, payment of salaries and internal costs clearly satisfied obligations of the contractors, not of the United States (Petition, App. B, 18a-19a). Furthermore, to the extent many states' tax structures do not tax receipts related to such expenditures, this case will not have the far-ranging impact claimed by the United States (Petition, 7).

United States v. Tax Commission of Mississippi, 421 U.S. 599 (1975); *Gurley v. Rhoden*, 421 U.S. 200 (1975); and *First Agricultural National Bank v. State Tax Commission*, 392 U.S. 339 (1968).

The present Petition affords no opportunity to reexamine or expand the doctrines enunciated in these cases. The United States raises no claim that the New Mexico taxes by their terms fall on the United States. Indeed, a companion case involving the same parties has already determined the opposite and was not appealed beyond the Tenth Circuit, *United States v. New Mexico*, 581 F.2d 803 (10th Cir. 1978).

Instead, the United States claims that the New Mexico taxes fall on the United States by virtue of contractual clauses which create agency relationships with its contractors. Consideration of this claim will of course have no relevance in states whose tax structures already place legal incidence on the United States statutorily, effectively exempting its contractors from those states' taxes.

But even the claims of agency are shopworn. *United States v. Boyd*, 378 U.S. 39 (1964) has already determined that AEC contractors are neither agents nor instrumentalities by virtue of general contract provisions and funding arrangements, albeit in regard to a use tax, not a gross receipts tax. The United States is simply trying to "shoe horn" the facts of this case into one of several established, and clearly inapposite, exceptions to the general taxability of federal contractors. No new ground will be broken if certiorari is granted.

2. In *Kern-Limerick, Inc. v. Scurlock*, 347 U.S. 110 (1954), this Court recognized the power of the executive branch to insulate its contractors from state taxes by explicitly designating them in all pertinent documents as procurement agents with

authority to pledge the credit of the United States.* The United States alleges a conflict between the *Kern-Limerick* holding and the present decision (Petition, 9-11). In fact, the decision of the Tenth Circuit accords a thoughtfully orthodox deference to the *Kern-Limerick* holding:

> . . . under *Kern-Limerick* a federal agency may bring a contractor within the scope of intergovernmental immunity if a decision to create an agency relationship is made in advance of a dispute and is unequivocably expressed in all relevant documents.
> (Petition, App. B, 17a).

The Tenth Circuit for good reason refused to accord any weight to certain contract modifications which referred directly to the contractors as agents (Petition, App. B, 25a). This refusal was based, first, on the fact that the modifications themselves contained crucial qualifiers: they did not "modify any other provisions of the contract" nor "create rights or obligations not otherwise provided for in the contract" (Petition, App. B, 26(a). Clearly, the modifications were a classic case of doublespeak. Since "the provisions of the contracts before the amendments did not establish agency status", the court was not swayed "by amendments which make no changes" (Petition, App. B, 26a).

Second, the modifications were inserted by low-level ERDA officials two years after this tax case commenced (Petition, App. B, 25a) and purported to be retrospective in application (Petition, App. A, 6a). Third, the contractors' purchase orders were not modified and continued to distinguish between the "Buyer" – Sandia, Zia or LACI – and the "Government" (Petition, App. B, 26a). Finally, although not stressed by the Tenth Circuit in the context of the modifications, the United States continued

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* Interestingly, at least one major federal agency, the Department of Defense, has as a matter of policy declined to exercise this power, refusing to insert "agency-creating clauses to avoid state and local taxes otherwise payable by its contractors", *United States v. New Mexico*, 581 F.2d 803, 808, n.1 (10th Cir. 1978).

to concede that these contractors were not federal instrumentalities, were not federal agents in day-to-day operations and were separate entities with their own employees (Petition, App. B, 18a, n.6; 21a).

The *Kern-Limerick* decision accorded to the executive branch a power equal to that of Congress in insulating federal contractors. It does not require the time of this Court to determine that the purported exercise of that power here was transparent and inadequate, falling far short of the *Kern-Limerick* requirements.

The United States further claims that the Tenth Circuit departed from *Kern-Limerick* in failing to read an agency relationship into the contractors' reliance on advanced funding (Petition, 9-11). It is the United States' position which conflicts with *Kern-Limerick*. A comparison of *Kern-Limerick* with the virtually identical facts in *Alabama v. King & Boozer*, supra, evidences this Court's refusal to "read between the lines" and divine an agency relationship from standard government contract clauses which stop short of explicit agency creation.

Directly on point, in *United States v. Boyd*, 378 U.S. 39 (1964), AEC management contractors were held to be neither federal instrumentalities nor agents exempt from the Tennessee use tax, although they relied on "Government funds" for all their costs (the same advanced funding put forward here), operated within an AEC facility, passed title to their purchases directly to the United States, secured advance approval of purchases from the United States, and were supervised and controlled by the United States, at 41-42, 46, 48.* The Court characterized the contractors as "cost-plus-fixed-fee" contractors despite their reliance on advanced funds, noted that their limited risk was a common characteristic of government contract-

* The United States' claim that a use tax is distinct from a gross receipts tax (Petition, 12, n.1) misses the point. Regardless of the *measure* of the Tennessee tax it would ultimately be *paid* from the same source as the New Mexico gross receipts tax, namely, the contractors' advanced funds accounts. If the Tennessee contractors were federal agents in disbursing

Cont. on p. 13

ing and observed that if the government wanted to utilize tax-exempt servants or its own employees, "it is well aware that it may do so and familiar with the ways of doing it", 378 U.S. at 46, 48.

As in *Boyd*, this Court is asked to read an agency relationship into "standard Atomic Energy Commission (now DOE) management contracts" (Petition, 2). The United States' claim that the contractors are agents in disbursing funds is negated by its concession that they are not agents for day-to-day operations (Petition, App. B, 12a, 18a, n.6). It is sophistry to claim the contractors are not agents when they *do* their work but are agents when they get *paid* for it. If these three contractors are agents by virtue of advanced funding, then so are the other 163 ERDA contractors similarly financed (Petition, App. B, n.10). This would frustrate the congressional intent in amending the Atomic Energy Act to "place Atomic Energy Commission contractors on the same footing as other contractors performing work for the Government", *United States v. Boyd*, 378 U.S. 39, 40 (1964). Furthermore, if these three contractors are agents, then so are the 8,000 contractors receiving advanced funding from other agencies, many of whom are elements of state and local government, 31 C.F.R. § 205.3(a) (1979) (Petition, App. B, 23a, 24a, n.10). The absurdity of this result mandates its rejection out of hand.

3. The United States alleges a conflict between the present decision and the decision of the Tennessee Supreme Court in the sales tax portion of *United States v. Boyd* which was not appealed to this Court, 211 Tenn. 139, 363 S.W.2d 193 (1962) (Petition, 12). In finding the contractors to be tax-exempt

Cont. from p. 12

from these accounts, the very claim made here (Petition, 10), the incidence of that tax would impermissibly fall on the United States through its agent. In finding the contractors in *Boyd* to be taxable, this Court implicitly rejected the notion that they functioned as disbursement agents in meeting their obligations with advanced funds.

procurement agents, the Tennessee Supreme Court found compliance with *Kern-Limerick, Inc. v. Scurlock* although the contractors were not designated as "purchasing agents", 363 S.W.2d at 200. This is hardly surprising since the contractors' purchase orders stated that they were placed "for and on behalf of the Government" and that "nothing herein shall preclude liability of the Government for any payment properly due hereunder", 363 S.W.2d at 199. These explicit authorizations to pledge the credit of the United States contrast sharply with the present case in which standard advanced funding arrangements are claimed to prove agency. There is no conflict in the law applied in the two cases, only a radical difference in the critical facts.

4. The United States alleges a conflict between the present decision and the decision of the Ninth Circuit in *United States v. Nevada Tax Commission*, 439 F.2d 435 (9th Cir. 1971), *aff'g* 291 F. Supp. 530 (1968). While the quote from the district court opinion at page 13 of the Petition is accurate, *that finding was not appealed to the Ninth Circuit.* All that was appealed was the *statutory* legal incidence of the Nevada tax in the wake of the recently decided *First Agricultural National Bank v. State Tax Commission*, 392 U.S. 339 (1968). The Ninth Circuit's treatment of the merits is confined to two short paragraphs, 439 F.2d at 441, which clearly state that only the statutorily-determined legal incidence was an issue on appeal. Indeed, the determination that the United States was the purchaser was *stipulated* by the parties on appeal, 439 F.2d at 439!

The Nevada district court opinion is devoid of the factual development here concerning the widespread use of advanced funds as well as the concessions that the contractors are neither instrumentalities nor day-to-day agents. In any event, a conflict between the Nevada district court and the Tenth Circuit is not a ground for granting certiorari, Supreme Court Rule 19; Stern and Gressman, *Supreme Court Practice* (4th ed. 1969), 161-162.

5. The United States claims a conflict between the present decision and *Livingston v. United States*, 179 F. Supp. 9 (E.D.S.C. 1959), *aff'd per curiam*, 364 U.S. 281 (1960). The alleged conflict concerns the disparate tax treatment of du Pont which received a $1 fee and Sandia which receives no fee (Petition, 11). In fact, there is no conflict.

Following *United States v. Boyd*, 378 U.S. 39 (1964), the significance of the *Livingston* opinion was reduced to "the 'extraordinary' contractual relationship between du Pont and AEC at this plant. . ." and the "factual determination that du Pont received no benefits from the contract", 378 U.S. at 45, n.6. In the instant case, the record discloses significant monetary and business benefits to Sandia and its profit-making parent from undertaking this contract (Petition, App. B, 25a, n.12). Furthermore, the contracts here are concededly "standard" (Petition, 2) and not "extraordinary". Finally, ERDA's regulations reveal that a contractor's fee is now a matter of negotiation, having nothing to do with the contractor's "high sense of public responsibility", *Livingston, supra*, at 23. (Petition, App. B, 25a). In summary, there is no conflict of law between *Livingston* and the present case, but only significant factual differences.

CONCLUSION

The petition for a writ of certiorari should be denied.

Respectfully submitted,

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January, 1981

APPENDIX A – 41 U.S.C. §255

Advance or other payments; restrictions; conditions

(a) Any executive agency may–

(1) make advance, partial, progress or other payments under contracts for property or services made by the agency; and

(2) insert in bid solicitations for procurement of property or services a provision limiting to small business concerns advance or progress payments.

(b) Payments made under subsection (a) of this section may not exceed the unpaid contract price.

(c) Advance payments under subsection (a) of this section may be made only upon adequate security and a determination by the agency head that to do so would be in the public interest. Such security may be in the form of a lien in favor of the Government on the property contracted for, on the balance in an account in which such payments are deposited, and on such of the property acquired for performance of the contract as the parties may agree. This lien shall be paramount to all other liens.

APPENDIX B – 31 C.F.R. Part 205 (1979)

WITHDRAWAL OF CASH FROM THE TREASURY FOR ADVANCES UNDER FEDERAL GRANT AND OTHER PROGRAMS

§ 205.1 Purpose.

This part prescribes the regulations governing advances to recipient organizations for financing operations under Federal grant and other programs.

§ 205.2 Scope of regulations.

(a) The regulations in this part apply to any Federal program requiring advances to finance the recipient organization's activities in carrying out the program, whether by contract, grant, contribution, or other form of agreement. (Advance payments on procurement contracts are also subject to the provisions of the Federal Procurement Regulations regarding contract financing which appear at 41 CFR 1-30 and the provisions of the Armed Services Procurement Regulations regarding defense contracting which appear at 32 CFR 163.) The regulations in this part are not generally applicable to loan programs. However, the letter-of-credit method should be considered by Federal program agencies for application to loans carrying interest rates which are lower than Treasury borrowing rates.

(b) These regulations are not intended to apply to Government disbursements made to reimburse an organization for work already performed and financed with the organization's own working capital. However, these regulations do apply to reimbursable grant programs involving nonprofit organizations participating in the single letter-of-credit funding technique. Any other specific application of features of these regulations to reimbursement payments will be considered by the Department of the Treasury if requested by a Federal program agency.

§ 205.3 Definitions.

For the purpose of this part:

(a) *Recipient organization* means an organization outside the Federal Government (including any State and local government, educational institution, international organization and any other public and private organization) receiving cash advances under Federal grant and other programs.

(b) *Primary recipient organization* means a recipient organization receiving cash advances directly from the Federal Government.

(c) *Secondary recipient organization* means a recipient organization receiving cash advances from a primary recipient organization.

(d) *Direct Treasury check* means the method whereby payment is made directly to a recipient organization by Treasury check authorized by the responsible officer of the Federal program agency.

(e) *Letter of Credit–Treasury Regional Disbursing Office System* means the system whereby the letters of credit are maintained and serviced by Treasury disbursing centers and Treasury regional disbursing offices.

(f) *Letter of Credit–Federal Reserve Bank System* means the system whereby the letters of credit are maintained and serviced by Federal Reserve banks and branches.

(g) *Checks paid technique* means the procedure whereby the drawdown on the letter of credit is delayed until the checks issued for program disbursements are presented to the recipient organization's bank for payment.

(h) *Delay of drawdown technique* means the procedure whereby the drawdown on the letter of credit is delayed until after checks issued for program disbursements have been forwarded to the payees.

(i) *Consolidation of funding to the same recipient organization under one letter of credit* means the procedure whereby, within a single accounting entity, the Federal program agency combines all advance funding to the same recipient organization

under one letter of credit. It [sic] achieving this objective, the Federal program agency shall include all advance funding to the recipient organization including that which ordinarily would not qualify because it does not meet the criteria established for the letter-of-credit method.

(j) *Single letter-of-credit technique* means the procedure whereby numerous letters of credit issued by different accounting entities within the same Federal department to State agencies, local government agencies, or recipient institutions are replaced by one centrally administered single letter of credit issued to one central organization within that State, local government, or recipient institution.

(k) *Working capital advance basis* means the procedure whereby funds are advanced to the recipient organization to cover its estimated disbursement needs for a given initial period. Thereafter, the recipient organization would be reimbursed for the amount of its actual cash disbursements. The amount of the initial advance shall be geared to the reimbursement cycle so that after the initial period the payments are approximately equal to the average amount of the recipient organization's unreimbursed program payments.

§ 205.4 General regulations.

(a) Cash advances to a recipient organization shall be limited to the minimum amounts needed and shall be timed to be in accord only with the actual, immediate cash requirements of the recipient organization in carrying out the purpose of the approved program or project. The timing and amount of cash advances shall be as close as is administratively feasible to the actual disbursements by the recipient organization for direct program costs and the proportionate share of any allowable indirect costs.

(b) If a Federal program agency has, or expects to have, a continuing relationship with a recipient organization for at least one year, involving annual advances aggregating at least $120,000,

the agency shall use the letter-of-credit method. Letters of credit will be established with the Treasury disbursing centers and Treasury regional disbursing offices (Letter of Credit–Treasury Regional Disbursing Office System) or the Federal Reserve banks and branches (Letter of Credit–Federal Reserve Bank System) as determined by the Commissioner, Bureau of Government Financial Operations, or his designee.

(c) When annual advances to a recipient organization aggregate less than $120,000 or there is not a continuing relationship for at least one year, the cash advances shall ordinarily be made by the direct Treasury check method. Such cash advances shall be made only in amounts necessary to meet current disbursement needs and shall be scheduled so that the funds are available to the recipient organization only immediately prior to their disbursement by the organization.

(d) Each Federal program agency shall work toward the objective of the consolidation of funding to the same recipient organization under one letter of credit. Also, the single letter-of-credit, checks paid, and the delay of drawdown techniques of withdrawing funds under the letter-of-credit method shall be employed wherever feasible under the direction and approval of the Department of the Treasury.

(e) Cash advances made by primary recipient organizations to secondary recipient organizations shall conform substantially to the same standards of timing and amount as apply to cash advances by Federal program agencies to primary recipient organizations. Federal program agencies shall require primary recipient organizations to develop procedures whereby secondary recipient organizations can obtain funds from the primary recipient organization as needed for disbursement.

§ 205.5 Irrevocability of the letter of credit.

A letter of credit is irrevocable (the equivalent of cash available to the recipient organization) to the extent the recipient organization has obligated funds in good faith thereunder in

executing the authorized Federal program in accordance with the grant, contract, or other agreement.

§ 205.6 Contract or grant provisions.

Use of letters of credit shall be covered by a clause in the grant, contract, or other financing agreement whereby the recipient organization commits itself to (a) initiating cash drawdowns only when actually needed for its disbursements, (b) timely reporting of cash disbursements and balances as required by the Federal program agency, and (c) the imposition of the same standards of timing and amount upon any secondary recipient organizations including the furnishing of reports of cash disbursements and balances, with the understanding that failure to adhere to these provisions may cause the unobligated portion of the letter of credit to be revoked by the Federal program agency or by the Department of the Treasury. The financial management system of the recipient organization shall provide for effective control over and accountability for all Federal funds as stated in OMB Circular A-102 revised for State and local governments and OMB Circular A-110 for institutions of higher education, hospitals, and other nonprofit organizations.

§ 205.7 Termination of advance methods of financing grant programs.

When a recipient organization receiving cash advances by a letter of credit or by direct Treasury check method has demonstrated to a Federal program agency an unwillingness or inability to establish procedures that will minimize the time elapsing between cash advances and the disbursement thereof, the Federal program agency, unless prohibited by the statutes governing the programs(s) in question, shall terminate advance financing and shall require the recipient organization to finance its operations with its own working capital, and payments to the recipient organization shall be made by direct Treasury check method to reimburse it for actual cash disbursements. In those cases in which the reimbursement method is not feasible,

arrangements may be made whereby the operations of the recipient organization are financed on a working capital advance basis.

§ 205.8 Responsibilities of Federal program agencies.

Regardless of the particular method used to advance funds, the Federal program agency shall be responsible for (a) making such reviews of the financial practices of recipient organizations, both primary and secondary, as are necessary to insure that the provisions of this part are being complied with, and (b) instituting such remedial measures as may be necessary in the event that a recipient organization demonstrates its unwillingness or inability to comply with these provisions. Federal program agencies shall formulate procedural instructions which specify the methods employed to carry out these responsibilities and shall forward copies of such instructions to the Commissioner, Bureau of Government Financial Operations, or his designee for approval. Also, each Federal program agency shall furnish the Department of the Treasury such periodic reports showing cash balances in the hands of the recipient organizations and results of reviews of the financial practices of recipient organizations as are required by the Commissioner, Bureau of Government Financial Operations, or his designee.

§ 205.9 Implementing instructions.

The Commissioner, Bureau of Government Financial Operations, will issue implementing instructions for the regulations established by this part in Volume I of the Treasury Fiscal Requirements Manual.

§ 205.10 Waivers.

Any waivers of the provisions of this part previously granted to Federal program agencies are hereby revoked. Requests for waivers of specific provisions of this part shall be presented in writing to the Commissioner, Bureau of Government Financial Operations, or his designee.

APPENDIX C – Section 4(c)(2) of the Atomic Energy Act of 1946, 60 Stat. 755, now codified at 42 U.S.C. § 2061(b)

OPERATION OF THE COMMISSION'S PRODUCTION FACILITIES.– The Commission is authorized and directed to produce or to provide for the production of fissionable material in its own facilities. To the extent deemed necessary, the Commission is authorized to make, or to continue in effect, contracts with persons obligating them to produce fissionable material in facilities owned by the Commission. The Commission is also authorized to enter into research and development contracts authorizing the contractor to produce fissionable material in facilities owned by the Commission to the extent that the production of such fissionable material may be incident to the conduct of research and development activities under such contracts. Any contract entered into under this section shall contain provisions (A) prohibiting the contractor with the Commission from subcontracting any part of the work he is obligated to perform under the contract, except as authorized by the Commission, and (B) obligating the contractor to make such reports to the Commission as it may deem appropriate with respect to his activities under the contract, to submit to frequent inspection by employees of the Commission of all such activities, and to comply with all safety and security regulations which may be prescribed by the Commission. Any contract made under the provisions of this paragraph may be made without regard to the provisions of section 3709 of the Revised Statutes (U.S.C., title 41, sec. 5) upon certification by the Commission that such action is necessary in the interest of the common defense and security, or upon a showing that advertising is not reasonably practicable, and partial and advance payments may be made under such contracts. The President shall determine at least once each year the quantities of fissionable material to be produced under this paragraph.

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No. 80-702

In the Supreme Court of the United States

OCTOBER TERM, 1980

UNITED STATES OF AMERICA, PETITIONER

v.

STATE OF NEW MEXICO, ET AL.

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE TENTH CIRCUIT

BRIEF FOR THE UNITED STATES

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QUESTION PRESENTED

Whether contractors of the United States Department of Energy, engaged to manage and operate government-owned atomic research laboratories, are procurement agents of the United States, so that payments made by the contractors with the federal government's funds, to procure goods and to pay for the operational costs of the laboratories, are constitutionally immune from the New Mexico gross receipts and compensating use taxes.*

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* In addition to the State of New Mexico, the other respondents in this case are the Bureau of Revenue of the State of New Mexico, and Fred L. O'Cheskey, as Commissioner of Revenue of and for the State of New Mexico.

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§ 72-16A-14 ..... 2, 4a
§ 72-16A-14.9 ..... 2, 4a

Miscellaneous:

Hiestand and Florsheim, *The AEC Management Contract Concept*, 29 Fed. Bar J. 67 (1969)..... 3
S. Rep. No. 694, 83d Cong., 1st Sess. (1953) 27

In the Supreme Court of the United States

OCTOBER TERM, 1980

No. 80-702

UNITED STATES OF AMERICA, PETITIONER

v.

STATE OF NEW MEXICO, ET AL.

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE TENTH CIRCUIT

BRIEF FOR THE UNITED STATES

OPINIONS BELOW

The opinion of the district court (Pet. App. 1a-10a) is reported at 455 F. Supp. 993. The opinion of the court of appeals (Pet. App. 11a-28a) is reported at 624 F.2d 111.

JURISDICTION

The judgment of the court of appeals (Pet. App. 29a-30a) was entered on June 2, 1980. By orders of August 15 and September 19, 1980, Mr. Justice White extended the time within which a petition for

a writ of certiorari could be filed to and including October 30, 1980. The petition for a writ of certiorari was filed on October 30, 1980, and granted on February 23, 1981. The jurisdiction of this Court rests on 28 U.S.C. 1254(1).

STATUTE INVOLVED

The pertinent parts of New Mexico's Gross Receipts and Compensating Tax Act, N.M. Stat. Ann. 1953, §§ 72-16A-3, 72-16A-4, 72-16A-7, 72-16A-12, 72-16A-12.1, 72-16A-12.2, 72-16A-14, and 72-16A-14.9 (Supp. 1975), are set forth in the App., *infra*, 1a-4a.

STATEMENT

1. Sandia Corporation was organized in 1949 as a special subsidiary of Western Electric Company, Inc., for the purposes of performing research and development for the United States Atomic Energy Commission (now the Department of Energy (DOE)) in New Mexico (Pet. App. 14a). It is not involved in any private work, receives no fee or profit under its contract, and owns no property except the $1,000 in United States bonds that constitutes its paid-in capital (Pet. App. 3a).

The Zia Company is a subsidiary of Santa Fe Industries, Inc. Since 1946, Zia has performed a variety of management, operational, maintenance, architect-engineer, procurement, and related functions in connection with DOE's Los Alamos Scientific Laboratory (Pet. App. 14a). Zia performs separate private work with a distinct set of records, employees and locations. Virtually none of Zia's private prop-

erty is involved in performance of its contract with DOE (Pet. App. 3a, 14a).

Los Alamos Constructors, Inc. (LACI) is a subsidiary of the Zia Company. It is devoted exclusively to the performance of construction work in support of the Los Alamos Scientific Laboratory, a government-owned research and development facility (J.A. 22-29).[1] LACI owns no tangible personal property and makes no purchases. Rather, it procures the property it needs for performance of its Los Alamos contract through Zia. All of LACI's activities are managed by its parent Zia. Zia and LACI are paid fixed fees annually for work performed under their contracts with DOE (Pet. App. 3a-4a, 14a).

The management contracts between DOE and Sandia, Zia, and LACI are standard Atomic Energy Commission (now DOE) management contracts. This type of contract was developed to facilitate the Atomic Energy Commission's substantial reliance upon private industry in the construction and management of large research and development facilities (Pet. App. 13a).[2] The standard DOE atomic facility management contract provides that title to all tangible personal property passes directly to the government from the vendor. Thus, the contractors do not own any of the tangible personal property they procure. Moreover, the contract also places the risk of loss upon the government for property procured under the contracts. Finally, the contract provides for government control over the disposition of the property and government approval of property management procedures employed by each contractor (Pet. App. 4a).

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[1] "J.A." refers to the Record Appendix.

[2] See generally Hiestand and Florsheim, *The AEC Management Contract Concept*, 29 Fed. Bar J. 67 (1969).

The tangible personal property procured by Sandia and Zia and all other operational costs incurred under the contracts, such as salaries, are paid for under an "advanced funding" procedure. Under this procedure, the contractors pay vendors and employees with drafts drawn directly on United States Treasury funds maintained in a depository bank account, under the authority of a letter of credit to cover withdrawals (Pet. App. 4a) (J.A. 19, 26).

The "advanced funding" procedure employs a special bank account established by the contractor, the United States, and a designated bank, pursuant to a three-party contract (J.A. 84-85b, 86-88, 89-90a, 92, 95, 96, 109-113). The United States owns any balance in the account (J.A. 19-20), but the contractor has the right to execute drafts payable to third parties in order to pay any expenses incurred in performing the underlying government contract. DOE thereupon issues a letter of credit to an appropriate Federal Reserve Bank in favor of the contractor. The letter of credit provides the general authority for the Federal Reserve Bank to make United States Treasury funds available for deposit in the special bank account (J.A. 95, 96). When a contractor incurs an expense under the contract, it pays the expense by executing a draft payable to the creditor and drawn on the special bank account. At the same time, the contractor or the bank executes a payment voucher in an amount sufficient to cover the draft and the Federal Reserve Bank, on the basis of the voucher, transfers funds into the special bank account (J.A. 109-113) (Pet. App. 22a n.8).

Under the contract, the government owns the funds in the special accounts and controls the disposition of such funds (J.A. 19, 26, 32-33). The liability

provisions of the contract require the government to pay all operational costs and further stipulate that no contractor funds are to be used to pay for contract costs. Obligations that are "properly incurred" by the contractors are therefore treated as DOE liabilities. Hence, if the government failed to provide funding, the contractors would be excused from performance of the contracts and the government would be liable for all properly incurred and reported claims (Pet. App. 4a-5a).

Prior to July 1, 1977, DOE's contracts with Sandia, Zia, and LACI did not refer to the contractors as "agents" of the government. On that date (which was during the pendency of this litigation), the contracts were modified to specify that the contractors are "agents for and on behalf of ERDA for certain purposes" (Pet. App. 26a), in recognition of the "long standing agency status and authority" of the contractors (Pet. App. 6a; J.A. 49-61). The amendments also stated that they "shall not be construed to modify any other provisions of the contract * * * nor shall [they] create rights or obligations not otherwise provided for in the contract" (Pet. App. 26a).

2. The New Mexico gross receipts tax is levied upon the gross receipts realized by persons engaged in the construction business or in performing services of a professional, technical, or scientific nature. There is also a compensating use tax equivalent to the gross receipts (sales) tax that is imposed upon the use of tangible personal property that has been imported into and used within the State without the payment of any gross receipts (sales) taxes. See App., *infra*, 1a-4a.

Prior to 1967, the New Mexico Bureau of Revenue acknowledged that the contractors engaged under the standard Atomic Energy Commission contracts were agents of the United States. The State therefore did not impose any taxes on the type of transactions involved in this case. In 1967, however, the State changed its position with respect to the relationship between the contractors and the government and sought to impose such taxes on the ground that the contractors were not agents of the United States (Pet. App. 6a). The State of New Mexico thereupon assessed gross receipts and compensating use taxes against Zia and LACI for the period January 1, 1966, through June 30, 1967, with respect to their disbursement of government funds and their out-of-state procurement of tangible personal property. After the State Commissioner of Revenue upheld the assessments, the United States and the contractors appealed to the Court of Appeals of New Mexico.[3] The New Mexico Court of Appeals reversed the Commissioner of Revenue's determination imposing gross receipts and compensating use taxes on the contractors' disbursement of federal funds and purchasing of tangible property. See *United States* v. *Bureau of Revenue*, 87 N.M. 164, 531 P.2d 212 (1975). It held that the Commissioner was estopped to assess the taxes in question because of his previous rulings that the contractors were agents of the United States and therefore immune from state taxation on their expenditures made with the federal government's funds. A concurring judge concluded that even on the as-

[3] The government and the contractors conceded liability for the gross receipts tax on the annual fixed fees paid as compensation for the contractors' services. Accordingly, those fees are not at issue in this case.

sumption that estoppel was unavailable, the New Mexico taxes could not be imposed upon the contractors' disbursements and purchases (see 87 N.M. at 166-170; 531 P.2d at 215-218).

Following the decision of the New Mexico Court of Appeals, the DOE requested the New Mexico Commissioner of Revenue, by letter dated January 30, 1975, to concede that contractors such as Zia and LACI were not liable for the gross receipts and compensating use taxes on their disbursements and procurements, and to authorize the contractors to issue permanent nontaxable transaction certificates in purchasing tangible personal property (J.A. 13-15). On February 28, 1975, the New Mexico Commissioner advised DOE that he refused to do so "until the courts finally address the important questions involved." In the State Commissioner's view, the New Mexico Court of Appeals' estoppel ruling had not resolved the substantive tax immunity issue and therefore another test case was necessary (J.A. 16-17).

3. Accordingly, on July 17, 1975, the government brought this action against the State of New Mexico in the United States District Court for the District of New Mexico for a declaratory judgment that sales of tangible personal property to DOE, through its management contractors Sandia and Zia, are sales to the United States that are exempt from the New Mexico gross receipts and compensating taxes, and that the advanced funds disbursed under the management contracts here are not subject to such taxes (Pet. App. 1a-2a, 11a-12a; J.A. 6-12).

The district court concluded "that Sandia and Zia are procurement agents of the United States and that any sales of tangible personal property to them are sales to the United States through its procure-

ment agents, which are not subject to the 4% gross receipts tax imposed by the New Mexico Gross Receipts and Compensating Tax Act" (Pet. App. 7a). It also held that the contractors are not subject to the compensating tax for their purchases of tangible personal property in other states (*ibid.*).

The district court further held that the advanced funds disbursed by Sandia, Zia and LACI are not compensation for services subject to the New Mexico gross receipts tax, but are funds that belonged to the government and were disbursed by the contractors to pay operational costs. In support of this conclusion, the district court observed that Zia and LACI received a fixed fee as compensation for their services, upon which they paid gross receipts taxes, and that Sandia received no fixed fee or profit. Moreover, the court pointed out that under the advanced funds procedure, the funds deposited by DOE in the special bank accounts were the only monies available for payment of all the contractors' operational costs. Those funds were not to be disbursed in any manner inconsistent with contract performance. DOE could exert direct control over the disbursement of the funds and retained title to the funds while they were on deposit with the bank (Pet. App. 8a-9a). Accordingly, the district court upheld the government contractors' immunity from New Mexico gross receipts and compensating use taxes and entered a declaratory judgment in favor of the government (Pet. App. 10a).

Finally, the district court rejected the State's argument that DOE had no authority to modify the contracts in 1977 to characterize Sandia, Zia and LACI as "agents." The court regarded the amendments to the contracts as simply confirming the na-

ture of the relationship that had always existed under the contracts. As the district court stated, "the Government and the contractors herein maintained an agency relationship for procurement purposes during the years of operation prior to the contract modifications, and have continued to do so to the present. They were not taxable before the modifications, because such modifications merely made the relationship more express, but did not change the agency relationship which had been in operation for three decades, and which had been recognized as such by the Bureau [of Revenue]" (Pet. App. 6a).

4. The court of appeals reversed (Pet. App. 11a-26a).[4] It held that Sandia, Zia, and LACI were not agents of the United States and were therefore subject to New Mexico gross receipts and compensating use taxes. After reviewing this Court's decisions dealing with the state tax immunity of government contractors, the court of appeals acknowledged that "[a]lthough there is language in these Supreme Court opinions suggesting that the results turn on traditional agency principles * * * it seems evident that the Court is more concerned with preserving the delicate financial balance between our co-existing

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[4] In the district court, the State argued that the United States had no right to challenge the imposition of the taxes at issue because it was not the "taxpayer" (Pet. App. 2a). The district court held that because the contracts require the United States to pay all costs under the contracts including taxes, the federal government as the real party in interest was the appropriate party to challenge the taxes on the ground of its constitutional immunity (Pet. App. 9a-10a). See *United States* v. *Bureau of Revenue*, 291 F.2d 677 (10th Cir. 1961); *Marquardt Corp.* v. *Weber County*, 360 F.2d 168 (10th Cir. 1966). The court of appeals affirmed this aspect of the district court's ruling (Pet. App. 26a-27a).

sovereignties than with rigid adherence to agency law terminology" (Pet. App. 17a). The court of appeals further observed that "[t]he trend toward restricting tax immunities * * * reflects an awareness of the serious threat posed to state revenues by ballooning governmental dealings in the private sector" (*ibid.*).

In holding that the contractors were not agents, the court of appeals sought to distinguish two decisions of this Court, *Kern-Limerick, Inc.* v. *Scurlock*, 347 U.S. 110 (1954), and *Livingston* v. *United States*, 364 U.S. 281 (1960) (per curiam), aff'g 179 F. Supp. 9 (E.D. S.C. 1959) (three-judge court), both of which upheld the immunity of contractors from state sales taxes in comparable circumstances on the ground that they were agents of the government.

As the court of appeals viewed the matter, the language in the request for bids, the contract, and the purchase order in *Kern-Limerick* more "clearly and uniformly disclosed an intention for the government to be directly obligated to the vendor for the contractor's purchases" than did the documents here (Pet. App. 15a). Although the court attempted to distinguish *Livingston* on the ground that the contractor in that case earned no fee (*id.* at 16a), it acknowledged that in the present case Sandia likewise earned no fee. However, the court of appeals "decline[d] to hang agency status, and thereby the welfare of state treasuries, on the existence or amount of a fee" (*id.* at 25a).

Finally, the court below rejected the government's argument that the advanced funding procedure conclusively established that Sandia, Zia and LACI were procurement agents that pledged the credit of the

United States vis-a-vis the third-party vendors. In the court's view, "[a]dvanced funding is simply another means of reimbursement devised by accountants to eliminate major weaknesses in the government's bookkeeping practices" (*id.* at 23a). Accordingly, the court of appeals was unwilling to attribute any significance to the 1977 contract modifications that explicitly confirmed that Sandia, Zia, and LACI are "agents for and on behalf of ERDA for certain purposes" (Pet. App. 26a). As the court stated, "[b]ecause we are convinced that, as a matter of law, the provisions of the contracts before the amendments did not establish agency status, we need not be swayed by amendments which make no changes" (*ibid.*).

SUMMARY OF ARGUMENT

1. In *M'Culloch* v. *Maryland*, 17 U.S. (4 Wheat.) 316 (1819), this Court first announced the doctrine that the federal government is immune from state taxation. "[U]nshaken, rarely questioned * * * is the principle that possessions, institutions, and activities of the Federal Government itself in the absence of express congressional consent are not subject to any form of state taxation." *United States* v. *County of Allegheny*, 322 U.S. 174, 177 (1944). See also *Department of Employment* v. *United States*, 385 U.S. 355 (1966); *United States* v. *Tax Commission of Mississippi*, 421 U.S. 599, 612-613 (1975). Federal tax immunity is "the unavoidable consequence of that supremacy which the constitution has declared." *M'Culloch* v. *Maryland*, *supra*, 17 U.S. (4 Wheat.) at 436.

In determining the reaches of the federal government's constitutional immunity from state taxation,

this Court has often extended the doctrine to protect private contractors who act on behalf of the United States. Thus, prior to *James* v. *Dravo Contracting Co.*, 302 U.S. 134 (1937), and *Alabama* v. *King & Boozer*, 314 U.S. 1 (1941), it had been held that a private contractor could not be subject to state taxation in connection with his performance of a government contract if he could pass the cost of the tax on to the federal government. However, in *King & Boozer* the Court abandoned this "economic burden" test and ruled that federal sovereignty "does not spell immunity from paying the added costs, attributable to the taxation of those who furnish supplies to the Government and who have been granted no tax immunity" (314 U.S. at 9). There, however, the legal incidence of the tax was on the private vendors, and the contracts provided that the contractor was to purchase the materials in its own name and on its own credit. The government was not bound by the contractors' purchase contracts but would reimburse the contractor only after the goods were delivered and inspected. In those circumstances, the Court concluded that the government's prerogatives under the contracts did not confer upon the contractor the status of an agent empowered to pledge the credit of the United States (see *id.* at 13).

Kern-Limerick, Inc. v. *Scurlock*, 347 U.S. 110 (1954), employed the Court's earlier analysis in *King & Boozer* in holding that sales to a federal contractor was entitled to immunity from state sales tax if the contractor was an agent of the federal government empowered to pledge the credit of the United States. There, the Court held unconstitutional the Arkansas sales tax as applied to purchases by a government contractor under a cost-plus-fixed fee contract, where the pertinent documents made it clear

that the contractor was acting as a purchasing agent for the government, title to the goods purchased passed directly from the vendor to the government, and the government was directly liable for payment of the purchase price. Accordingly, the Court concluded that "the Government is the disclosed purchaser and that no liability of the purchasing agent to the seller arises from the transaction" (347 U.S. at 121; footnote omitted).

2. The decision below rejecting the claimed immunity of the contractors in this case is contrary to *Kern-Limerick*, which we submit controls this case. Here, as in *Kern-Limerick*, the DOE management contracts to which Sandia, Zia and LACI are parties provide that title to all tangible personal property passes directly to the government from the vendors, and place the risk of loss directly on the government for property acquired under the contracts. The contracts further provide for government control over the disposition of the property and approval of property management procedures employed by each contractor.

Finally, and most importantly, the advanced funding arrangement, under which the contractors do not expend any of their own funds for goods or services but are able to disburse monies that at all times belong to the government, "gave to the contractors the status of agents of the Government to enter into contracts or to pledge its credit." *Alabama* v. *King & Boozer*, *supra*, 314 U.S. at 13. As the Fourth Circuit correctly observed in *United States* v. *Forst*, 569 F.2d 811 (1978), "the key factor in the case was whether the credit of the United States or the contractor was bound by the purchasing agreements" (*id.* at 811). Since Sandia, Zia, and LACI were empowered to write checks on government-owned funds, their power to bind the United

States and pledge its credit cannot seriously be questioned.

Contrary to the court of appeals' conclusion, the advanced funding procedure cannot be dismissed as "simply another means of reimbursement devised by accountants * * *" (Pet. App. 23a). There is a considerable difference between the case where the contractor expends its own funds and must await reimbursement by the government and the case in which the contractor is empowered to draw directly on the funds of the government. While the former case may not be inconsistent with an agency relationship (as *Kern-Limerick* itself demonstrates), it is at least clear that in such a case the contractor must rely upon the government's ratification of its actions in order to obtain reimbursement for its outlays. Here, the contractors did not take even that risk, for they disbursed *government* funds to the vendors and to their employees in the first instance. In every sense of the word, the contractors here acted on behalf of the government vis-a-vis the vendors. If sales to a contractor receiving after-the-fact reimbursement in *Kern-Limerick* were deemed to be sales to an agent of the United States, and thereby immune from state taxes, there is a stronger case for immunity here because the contractors had the additional authority to disburse government-owned funds and pledge the credit of the United States.

Although the court of appeals acknowledged that the advanced funding procedure created "appearances" of agency status for the contractors (Pet. App. 22a), it resisted the conclusion that the contractors were immune from state taxes, relying on the fact that "[a]t most, the contractor may pledge to the limits of its letter of credit" (*id.* at 22a-23a).

As the court reasoned, "[s]een in this light, Sandia, Zia and LACI are like numerous businesses which deal under letters of credit from banks and other sureties" (*id.* at 23a).

But the conclusion that the contractors' purchases and disbursements were subject to state gross receipts taxes does not follow from the fact that their letters of credit were limited in amount. The claim of immunity here is only coextensive with the contractors' authority to act on behalf of the government. The fact that their authority, like the authority of many agents, was limited in dollar amounts does not refute the argument that they acted as agents of the government within the scope of their authority. Indeed, in *Livingston* v. *United States*, 364 U.S. 281 (1960), aff'g 179 F. Supp. 9 (E.D. S.C. 1959), this Court summarily affirmed a three-judge district court's decision that a South Carolina sales tax could not be imposed upon a contractor's purchases under a similar DOE standard management contract. The court of appeals sought to distinguish that case on the ground that it turned on the fact that the contractor earned no fee from the contract (Pet. App. 16a), in much the same fashion as this Court distinguished *Livingston* in *United States* v. *Boyd*, 378 U.S. 39, 45 n.6 (1964). However, the court of appeals also expressed doubt that "such a factual determination would today withstand appellate review" (Pet. App. 24a; footnote omitted) and therefore "decline[d] to hang agency status, and thereby the welfare of state treasuries, on the existence or amount of a fee" (*id.* at 25a).

But whatever the merits of such a distinction, the undisputed fact is that Sandia received no fee or profit under its contract with DOE (Pet. App. 3a).

At all events, the Court's distinction of *Livingston* in *Boyd* rests upon the assumption that the South Carolina tax in the former case was a "privilege"-type use tax comparable to the Tennessee use tax at issue in *Boyd*. Since it is undisputed that the New Mexico use tax is, by contrast, a compensating use tax designed to tax out-of-state purchases of property brought into the state, the fact that two of the contractors here earned a fee has no relevance.

3. Nor does the fact "that the agency terminology does not appear uniformly in all the documents relating to the contracts" (Pet. App. 26a) effectively distinguish this case from *Kern-Limerick*, as the court of appeals apparently believed. Much the same argument was advanced by the State of Tennessee and rejected by the Tennessee Supreme Court in *United States* v. *Boyd*, 211 Tenn. 139, 363 S.W.2d 193 (1962), aff'd on another issue, 378 U.S. 39 (1964). There, the Tennessee court held that the contractor under the identical standard DOE management contract with advanced funding was immune from state sales taxes. In response to the argument that the contract did not in all respects employ the identical *Kern-Limerick* terminology of "agency," the court stated, in terms that are equally appropriate here (211 Tenn. at 155; 363 S.W.2d at 200): "The mere placing of terms such as agent or independent contractor in the contract does not make them such in law. The surrounding facts and circumstances determine the relationship."

Finally, the court of appeals stated that it was "highly skeptical of the sporadic addition of 'magic words' to a contract in an attempt to avoid state taxation" (Pet. App. 26a). But the modifications to the contracts were simply designed to confirm the status of the contractors as procurement agents of the

United States. Indeed, this Court in *Kern-Limerick* specified that "the form of contracts, when governmental immunity is not waived by Congress, may determine the effect of state taxation on federal agencies, for decisions consistently prohibit taxes levied on the property or purchases of the Government itself" (347 U.S. at 122-123; footnotes omitted). The form of these standard DOE atomic management contracts establish the immunity of the contractors from New Mexico sales and use taxes.

ARGUMENT

THE CONTRACTORS HERE ARE PROCUREMENT AGENTS OF THE UNITED STATES AND HENCE PAYMENTS MADE BY THEM WITH THE FEDERAL GOVERNMENT'S FUNDS TO PROCURE GOODS AND TO PAY FOR THE OPERATIONAL COSTS UNDER THEIR CONTRACTS ARE CONSTITUTIONALLY IMMUNE FROM THE NEW MEXICO GROSS RECEIPTS AND COMPENSATING USE TAXES

A. The Supremacy Clause of the Constitution Immunizes the Federal Government and its Agents from State Taxation

At issue in this case is whether the federal government's constitutional immunity from state taxation protects a private contractor's disbursement of the federal government's funds—in connection with its performance of a standard Department of Energy contract for the management of a government-owned atomic facility—from state gross receipts and use taxes. We submit that under the standard DOE contract for the management of atomic research laboratories at issue here, such contractors are procurement agents of the United States and that their disburse-

ments of advanced funds and purchases of goods under the contract are therefore immune from state gross receipts and compensating use taxes in the same manner as if the purchases had been made directly by the federal government itself.

Article VI of the Constitution provides that "[t]his Constitution, and the Laws of the United States which shall be made in Pursuance thereof; * * * shall be the supreme Law of the Land; and the Judges in every State shall be bound thereby, any Thing in the Constitution or Laws of any State to the Contrary notwithstanding." In *M'Culloch* v. *Maryland*, 17 U.S. (4 Wheat.) 316 (1819), this Court first announced the doctrine that properties, functions, and instrumentalities of the federal government are immune from state taxation. "[U]nshaken, rarely questioned * * * is the principle that possessions, institutions, and activities of the Federal Government itself in the absence of express congressional consent are not subject to any form of state taxation." *United States* v. *County of Allegheny*, 322 U.S. 174, 177 (1944). See also *Department of Employment* v. *United States*, 385 U.S. 355, 358-359 (1966); *United States* v. *Tax Commission of Mississippi*, 421 U.S. 599, 612-613 (1975); *United States* v. *County of Fresno*, 429 U.S. 452, 459 (1977). Federal tax immunity is "the unavoidable consequence of that supremacy which the constitution has declared." *M'Culloch* v. *Maryland*, *supra*, 17 U.S. (4 Wheat.) at 436.

In establishing the scope of the federal government's immunity from state taxation, this Court has often accorded constitutional protection from such taxes to private contractors who act on behalf of the United States. At the outset, the immunity was broad and virtually absolute in every instance where the federal government was made to bear the addi-

tional cost of the state tax. Thus, prior to *James* v. *Dravo Contracting Co.*, 302 U.S. 134 (1937), and *Alabama* v. *King & Boozer*, 314 U.S. 1 (1941), the Court had held that a private contractor could not be subject to state taxation in connection with his performance of a government contract if he could pass the cost on to the federal government. See, *e.g.*, *Panhandle Oil Co.* v. *Knox*, 277 U.S. 218 (1928); *Graves* v. *Texas Co.*, 298 U.S. 393 (1936).

However, in *Dravo* and in *King & Boozer*, the Court abandoned this "economic burden" test and ruled that federal sovereignty "does not spell immunity from paying the added costs, attributable to the taxation of those who furnish supplies to the Government and who have been granted no tax immunity" (314 U.S. at 9). There, the legal incidence of the tax was on the contractors, and the contracts provided that the contractor was to purchase the materials in its own name and on its own credit. The government was not bound by the contractors' purchase contracts but would reimburse the contractor only after the goods were delivered and inspected. In those circumstances, the Court concluded that the government's prerogatives under the contracts did not confer upon the contractor the status of an agent empowered to pledge the credit of the United States (see *id.* at 13). As the Court observed in the companion case of *Curry* v. *United States*, 314 U.S. 14, 18 (1941), "the Constitution, without implementation by congressional legislation, does not prohibit a tax upon Government contractors because its burden is passed on economically by the terms of the contract or otherwise as a part of the construction cost to the Government."

Thirteen years later in *Kern-Limerick, Inc.* v. *Scurlock*, 347 U.S. 110 (1954), the Court employed the *King & Boozer* analysis in ruling that sales to a federal contractor were entitled to immunity from

state sales tax if the contractor was an agent of the federal government empowered to pledge the credit of the United States. There, the Court struck down as unconstitutional the Arkansas sales tax as applied to purchases by a government contractor under a cost-plus-fixed fee contract, where the pertinent documents made it clear that the contractor was acting as a purchasing agent for the government, that title to the goods passed directly from the vendor to the government, and that the government was directly liable for payment of the purchase price. The Court concluded that "the Government is the disclosed purchaser and that no liability of the purchasing agent to the seller arises from the transaction" (347 U.S. at 121; footnote omitted).

In our view, the agency principle established in *Kern-Limerick* controls this case. As we shall show (pages 28-40, *infra*), here, as in *Kern-Limerick*, the DOE management contracts to which Sandia, Zia and LACI are parties, provide that title to all tangible personal property passes directly to the government from the vendors, and place the risk of loss directly on the government for property acquired under the contracts. The contracts further provide for government control over the disposition of the property and approval of property management procedures employed by each contractor. Finally, the advanced funding arrangement, under which the contractors do not expend any of their own funds for goods or services but are able to disburse monies that at all times belonged to the government, "gave to the contractors the status of agents of the Government to enter into contracts or to pledge its credit." *Alabama* v. *King & Boozer*, *supra*, 314 U.S. at 13. That is the fundamental prerequisite for a government contractor's claim of federal tax immunity.

B. The Contracts Here Designate the Contractors as Procurement Agents of the United States Empowered to Disburse Funds Belonging to the Federal Government

1. As we have pointed out (pages 19-20, *supra*), in *Kern-Limerick, Inc.* v. *Scurlock, supra*, 347 U.S. at 122, the contractor *Kern-Limerick* had a cost-plus fixed fee contract with the Department of the Navy which provided that all purchases made under the contract were made by the Navy, with Kern-Limerick acting only as its agent. The State of Arkansas sought to impose its sales tax on the contractor's purchases. The Court held that the question of who was the purchaser for state tax purposes was a federal question, that the legal incidence of the tax was on the purchaser, that the Department of the Navy was the real purchaser, and that the tax was therefore invalid. As the Court there stated, "[w]e find that the purchaser under this contract was the United States" (*ibid.*).

In so ruling, the Court distinguished its prior decision in *Alabama* v. *King & Boozer, supra*, 314 U.S. at 11, where the contractual provisions "plainly contemplate that the contractors were to purchase in their own names and on their own credit all the materials required * * *; that the Government was not to be bound by their purchase contracts, but was obligated only to reimburse the contractors when the materials purchased should be delivered, inspected and accepted at the site." For a private contractor to be cloaked with the government's immunity from state taxation, it must be clear under the contract that it is an agent empowered to bind the government or to pledge its credit. Thus, in *Kern-Limerick*, the Court cited as "[t]he significant difference" (347 U.S. at 119) between that case and *King & Boozer*

that both Kern-Limerick's request for bids and its purchase order contained the following provision (*id.* at 119-120):

> 3. This purchase is made by the Government. The Government shall be obligated to the Vendor for the purchase price, but the Contractor shall handle all payments hereunder on behalf of the Government. The vendor agrees to make demand or claim for payment of the purchase price from the Government by submitting an invoice to the Contractor. Title to all materials and supplies purchased hereunder shall vest in the Government directly from the Vendor. The Contractor shall not acquire title to any thereof.

Moreover, the arrangement between Kern-Limerick and the government required specific government approval to the purchasing agent for each request for bid and each purchase. Accordingly, the Court concluded "that the Government [was] the disclosed purchaser and that no liability of the purchasing agent to the seller [arose] from the transaction" (*id.* at 121; footnote omitted).

2. In ruling that the contractors here are not immune from state gross receipts and use taxes, the court of appeals suggested (Pet. App. 15a-17a) that subsequent decisions of this Court have undermined the authority of *Kern-Limerick*. But that case continues to stand as the leading precedent in determining the circumstances under which a private contractor serves as an agent of the United States so that its purchasing activities on behalf of the government are immune from state sales taxes. Indeed, the Court followed *Kern-Limerick* in *Livingston* v. *United States*, 364 U.S. 281 (1960) (per curiam), aff'g 179 F. Supp. 9 (E.D. S.C. 1959), with which the decision below

cannot be squared. There, this Court summarily affirmed a three-judge district court's decision that a South Carolina sales tax could not be imposed upon a contractor's purchases under a management contract between the Atomic Energy Commission and duPont that is virtually identical to the contracts at issue here. As the district court there stated, in terms that are equally applicable here, "[d]uPont's credit was not to be advanced or risked. Its disclosures in its requests for quotation and its purchase orders that the goods were being procured for the United States, to whom title would directly pass, and its imposition of the terms required of public contracts with the United States negatived any individual liability of its own. What obligations did arise from the purchase orders were discharged by drawing directly upon public funds" (179 F. Supp. at 21; footnote omitted).

The court of appeals sought to distinguish *Livingston* on the ground that it turned on the fact that the contractor earned no fee from the contract (Pet. App. 16a), in much the same way as this Court distinguished *Livingston* in *United States* v. *Boyd*, 378 U.S. 39, 45 n.6 (1964). But whatever the merits of such a distinction, the undisputed fact is that Sandia likewise received no profit or fee under its contract (Pet. App. 3a). At all events, the court of appeals also expressed doubt that "such a factual determination would today withstand appellate review (*id.* at 24a; footnote omitted) and therefore "decline[d] to hang agency status, and thereby the welfare of state treasuries, on the existence or amount of a fee" (*id.* at 25a).

In our view, this Court's reference in *Boyd* to the fact that the contractor in *Livingston* earned no fee is best explained in the context of the question presented to this Court in *Boyd*, *i.e.*, the validity of a

Tennessee use tax on the privilege of using tangible personal property for profit and gain irrespective of the title of the property or its importation (see 378 U.S. at 40-41 n.3, 43).[5] Accordingly, the fact that the contractor in *Boyd* used government-owned property for its own commercial advantage and profit was a sufficient basis upon which the Court could uphold the Tennessee tax on the authority of the so-called "Michigan cases." See *United States* v. *City of Detroit*, 355 U.S. 466 (1958); *United States* v. *Township of Muskegon*, 355 U.S. 484 (1958).[6] Thus, to the extent that the Court in *Boyd* regarded the South Carolina use tax in *Livingston* as comparable to the Tennessee use tax (see 378 U.S. at 45 n.6), the fact that duPont received no fee in *Livingston* offered an additional ground for distinguishing that case. While we believe that the South Carolina use

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[5] The sales tax question in *Boyd* was litigated only through the Tennessee Supreme Court. As we discuss (pages 38-40, *infra*), that aspect of the case bears upon the New Mexico taxes at issue here.

[6] The "privilege"-type use tax is valid only to the extent it segregates the contractor's interest in the government-owned property. *United States* v. *State of Colorado*, 627 F.2d 217 (10th Cir. 1980), aff'd, No. 80-714 (Feb. 23, 1981). There, the court below held that a Colorado property tax upon a private contractor engaged to manage a federal atomic facility violated the federal government's constitutional immunity from state taxation, where such tax did not segregate whatever limited interest the contractor had in the use of the government-owned property to perform the contract but was based upon the fair market of the property. The county's failure to limit the tax to the contractor's interest was evidenced by the fact that the tax amounted to almost twice the contractor's fixed management fee. See also *United States* v. *County of Allegheny*, *supra*.

tax in *Livingston* is more properly viewed as a compensating use tax meant to complement a sales tax by levying a tax upon out-of-state purchases (see, *e.g.*, *General Trading Co.* v. *State Tax Commission*, 322 U.S. 335, 336-337 (1944)) and therefore different from the privilege-type use tax in *Boyd*, it has never been disputed that the New Mexico use tax at issue here is a compensating use tax. See *Mescalero Apache Tribe* v. *Jones*, 411 U.S. 145, 158 (1973). Hence, the fact that two of the contractors in this case (Zia and LACI) earned a fee has no relevance.[7] Moreover, given the difference between the use tax involved in *Boyd* and the New Mexico use tax in the instant case, the court of appeals' reliance (Pet. App. 20a n.7) upon this Court's use tax holding in *Boyd* is misplaced.

If any further demonstration of the viability of *Kern-Limerick* as a precedent is required, the Court's recent decision in *United States* v. *County of Fresno*, *supra*, 429 U.S. at 459-460 n.7, should conclusively settle the matter. While the Court in that case found *Kern-Limerick* to be distinguishable, it cited the case as standing only for the proposition that "the State may not impose a tax the legal incidence of which falls on the Federal Government."

It is precisely that proposition upon which we rely in challenging the validity of the state taxes at issue in this case. Here, it is undisputed that the legal incidence of both the New Mexico gross receipts and compensating use tax is on the contractors. Indeed, the court below so held in a prior case involving defense contracts that "specifically provide[d] that the contractors [were] not acting as agents of the United States." *United States* v. *State of New*

[7] The imposition of the New Mexico gross receipts tax on these fees is not in dispute. See page 6 note 3, *supra*.

Mexico, 581 F.2d 803, 806 (10th Cir. 1978). In so ruling, however, the court below acknowledged—citing *Kern-Limerick*—that "[i]f the United States desires to avoid enriching state coffers with federal funds, it can easily do so by changing the terms of its contracts" (*id.* at 808 n.1).[8]

We submit that the terms of the standard federal contract for the management of atomic facilities accomplish exactly that result in accordance with the guidelines established by this Court in *Kern-Limerick* and in *Livingston*, with reference to contracts indistinguishable from the instant arrangements.[9]

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[8] The court drew further support for its conclusion that the defense contractors in *United States* v. *State of New Mexico*, *supra*, were not agents of the United States from the trial court's finding "that at least since 1955, it has been the policy of the Department of Defense not to include in its contracts agency-creating clauses to avoid state and local taxes otherwise payable by its contractors" (581 F.2d at 808 n.1). See also *United States* v. *Forst*, 569 F.2d 811 (4th Cir. 1978).

[9] It is clear that *Kern-Limerick* is the pertinent precedent for determining whether contractors under the standard federal contract for the management of atomic facilities qualify for the constitutional immunity of the federal government from state and local taxation.

The origin of the particular management contract involved in this case derives from the arrangements to develop atomic weapons made during World War II between the federal government (through the Manhattan Engineering District) and various universities and industrial organizations. After the cessation of hostilities, the responsibilities of the Manhattan Engineering District were transferred to the Atomic Energy Commission by the Atomic Energy Act of 1946, ch. 724, 60 Stat. 755 *et seq.* The Atomic Energy Act of 1946 provided that the Atomic Energy Commission would be the sole owner of certain nuclear materials and the facilities to produce nuclear weapons, and directed the Commission to

Just as in *Kern-Limerick*, the standard atomic management contract clearly designates the contractor as a procurement agent of the United States so that

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contract for the operation of these facilities (Section 4(c)(1) and (2)). The Commission continued the practice of contracting with private parties under the Atomic Energy Act of 1954, 42 U.S.C. 2011 *et seq.* Accordingly, there has been a longstanding and unique partnership between the government and private industry arising from the government's monopoly of nuclear materiel production (see 42 U.S.C. 2061(a)) and industry's technical capacity to accomplish that production under government contract.

Congress was not unaware of the possibility that local governments might seek to tax the activities of contractors engaged by the Atomic Energy Commission. Thus, Section 9(b) of the 1946 Act expressly exempted the "property, activities, and income" of the Commission from local taxation. When this was eventually challenged as applied to the Commission's contractors, this Court in *Carson* v. *Roane-Anderson Co.*, 342 U.S. 232 (1952), held that two such contractors were performing "activities" for the Commission, and were exempt from local taxation. Accord, *General Electric Co.* v. *Washington*, 347 U.S. 909 (1954). Shortly after the *Carson* decision, Congress repealed Section 9(b), expressing the view that the Atomic Energy Commission and its contractors should be in the same position as other federal agencies with respect to immunity from state and local taxation. Act of August 13, 1953, ch. 432, 67 Stat. 575. See S. Rep. No. 694, 83d Cong., 1st Sess. (1953), discussed in *Kern-Limerick* v. *Scurlock*, *supra*, 347 U.S. at 117, and in *United States* v. *Boyd*, 378 U.S. 39, 49-50 & n.10 (1964). But as the Court pointed out in *Kern-Limerick*, *supra*, 347 U.S. at 117, "in recommending the legislation the Joint Committee on Atomic Energy, while providing for voluntary contributions, did not propose to subject Government property and purchases to state taxes. The enactment left them free. This recognition of the Constitutional immunity of the Federal Government from state exactions rests, of course, upon unquestioned authority" (footnote omitted).

the federal government was the disclosed purchaser.[10] Since the contractors here are disbursing and procuring agents of the government, the legal incidence of the New Mexico tax is on the government; hence, the tax cannot validly be imposed upon them.

Finally, in rejecting the government's claim of contractor immunity under the standard atomic facility management contract, the court of appeals observed that its "reiterated antipathy to wholesale deprivations of state treasuries without congressional action, requires, at the least, some special arrangement before tax immunity attaches" (Pet. App. 21a). But, as this Court demonstrated by its summary affirmance of the three-judge district court in *Livingston*, the advanced funding procedure employed under the contracts at issue constitutes the very type of "special arrangement" that effectively insulates these federal contractors from state sales and compensating use taxes. A detailed examination of the contracts between Sandia, Zia, and LACI and the Department of Energy, to which we now turn, establishes the tax immunity of the contractors in this case under the foregoing legal principles.

C. The Contractors in This Case Qualify for State Tax Immunity Under the Criteria Established in *Kern-Limerick, Inc.* v. *Scurlock*, 347 U.S. 110 (1954)

1. In *Kern-Limerick*, the Court cited the following facts to support its determination that sales to the contractor acting as a purchasing agent for the

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[10] The standard atomic management contract is therefore significantly different from the defense contracts at issue in *United States* v. *State of New Mexico, supra*. There is accordingly no basis for the court of appeals' characterization of the argument that Sandia, Zia, and LACI are procurement agents of the government as "at odds with the [defense] contracts discussed" in its own prior decision (Pet. App. 19a).

United States were therefore immune from state sales tax. First, title to all materials and supplies purchased vested in the government directly and the contractor never acquired any title to the goods (347 U.S. at 112 n.2, 119-120). Second, the contract required "specific Government approval to the purchasing agent for each request for bid and each purchase" (*id.* at 120; see also *id.* at 112 n.2). Third, the request for bids explicitly stated: "This purchase is made by the Government. The Government shall be obligated to the Vendor for the purchase price, but the Contractor shall handle all payments hereunder on behalf of the Government" (*id.* at 119). Finally, the contract provided that "[t]he Contractor shall act as the purchasing agent of the Government in effecting such procurement and the Government shall be directly liable to the vendors for the purchase price" (347 U.S. at 112 n.2). The Court therefore concluded that "[u]nder these circumstances, it is clear that the Government is the disclosed purchaser and that no liability of the purchasing agent to the seller arises from the transaction" (*id.* at 120-121; footnote omitted).

In sum, the purchasing agency relationship between the government and the contractor rested upon: (1) immediate passage of title from the vendor to the government; (2) governmental approval for purchases; (3) specific notice to the vendor that the purchase in question is being made by the government; and (4) explicit characterization of the contractor as a purchasing agent of the government. An examination of the contracts and other pertinent documents in the present case demonstrates that Zia, Sandia, and LACI all qualified for tax immunity as purchasing agents of the United States under the rule of *Kern-Limerick.*

a. *Title to Goods.* In accordance with each contract, "title to all materials, equipment, supplies, and tangible personal property of every kind and description purchased by the Contractor, for the cost of which the Contractor is entitled to be reimbursed as a direct item of cost under this contract, shall pass directly from the vendor to the Government" (J.A. 20b; see also 13, 231a (Zia); 34, 151 (Sandia);[11] 29 (LACI)). Hence, it cannot be seriously questioned that the direct passage of title from the vendor to the United States was precisely the same as in *Kern-Limerick.*

b. *Government controls.* Moreover, each of the contracts provides an extensive system of government controls over the contractors' activities that serves the same purpose as the required governmental approval for each purchase in *Kern-Limerick.* For example, each contractor is obligated to "prepare and submit annually as of June 30, a voucher, for the total of net expenditures accrued (i.e., net costs incurred) for the period covered by the voucher, and the [Atomic Energy] Commission, after audit and appropriate adjustment[,] will approve such voucher" (J.A. 20 (Zia); 27 (LACI)). See also J.A. 31-32 (Sandia) (written approval of Commission required for advances in excess of $15,000). In addition, the contractors are required to establish and maintain property management systems, bonding and insurance and financial plans with cost limitations, and to appoint key personnel acceptable to the gov-

[11] The passage-of-title clause in the Sandia contract employs somewhat different wording but the legal effect is the same. It provides: "Title to all property of any kind whatsoever acquired by Sandia Corporation shall pass to the Government when it passes from the vendor, except as may be directed by the Commission" (J.A. 34).

ernment (J.A. 21a (Zia); 22, 23-25 (LACI); 37, 46 (Sandia)). Moreover, any disputes under the contracts which were not resolved by the contractor and the vendor were to be resolved by the appropriate DOE contracting official (see J.A. 128-129, 157-158). Thus, while the contractors in this case operated with somewhat greater autonomy on a day-to-day basis than *Kern-Limerick*, they were likewise fully accountable to the government for their purchases and actions. The difference in governmental control between this case and *Kern-Limerick* is one of degree and not of kind. Moreover, this factor is not as significant here, in light of the advanced funding present in this case, but not in *Kern-Limerick* (see pages 32-35, *infra*).

c. *Notice of third parties.* Furthermore, the third-party vendors of goods and services in this case were equally aware that the dealings of Zia, Sandia, and LACI with them were on behalf of the United States. Just as the request for bids in *Kern-Limerick* explicitly advised the third party that "[t]his purchase is made by the Government" (347 U.S. at 119), here, too, the face of the contractors' checks specifically stated that they were drawn against government funds. Thus, Zia's checks bore the legend "A.E.C. ADVANCE FUNDS/PAYROLL ACCOUNT/NOT TO EXCEED $500" (Exh. 19, J.A. 99) or "U.S. ENERGY RESEARCH AND DEVELOPMNT ADMINISTRATION/ADVANCE FUNDS ACCOUNT" (Exh. 21, J.A. 101). Sandia's checks similarly stated: "SANDIA LABORATORIES/ALBUQUERQUE, NEW MEXICO 87115/OPERATED BY SANDIA CORPORATION/for/ENERGY RESEARCH AND DEVELOPMENT ADMINISTRATION/ADVANCE FUNDS ACCOUNT" (Exh. 20, J.A. 100).[12]

[12] The facts that there were earlier Sandia checks (Exh. 18, J.A. 97-98) and a LACI check (Exh. 19, J.A. 99)

d. *Characterization of the contractors as purchasing agents.* That the parties intended that Zia, Sandia, and LACI were to be purchasing agents of the government is demonstrated by the advanced funding arrangement and confirmed by the contract modifications.

(1) *Advance funding.* As we have pointed out (pages 4-5, *supra*), under the advanced funding procedure, the contractor, the United States, and a designated bank open a special bank account pursuant to a three-party contract (J.A. 111-113). The United States owns the balance in the account and all revenues under the contract are government property required to be deposited in the account. However, the contractor is empowered to issue drafts to third parties for expenses incurred under the contract (*id.* at 20, 26, 27, 82-83a, 84-90a). The general authority for the funding of the bank account originates in a letter of credit issued by DOE to the Federal Reserve Bank in favor of the contractor (*id.* at 82-83a, 92-93, 95, 96). When the contractor issues a check to a third party, it also issues a voucher, which it forwards to the Federal Reserve Bank. As a result,

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introduced into evidence that do not state on their face that they were drawn on government funds, does not cast substantial doubt upon our submission that the third party vendors were aware that all three contractors were acting on behalf of the government. Both Sandia and LACI were organized for the sole purpose of serving as government contractors. Neither was involved in any private work (see J.A. 31). Indeed, LACI (a subsidiary of Zia) was exclusively involved in construction work in support of the Los Alamos Scientific Laboratory, a government-owned facility. LACI owned no tangible personal property and procured all of the property it required from Zia (Pet. App. 3a, 14a). Hence, no third party could have been unaware that Sandia and LACI were procurement agents of the government.

the Federal Reserve Bank deposits an equivalent sum to the account of the designated bank of deposit, which in turn credits the special bank account with sufficient funds to cover the draft. See J.A. 81-83a, 91-94.

The foregoing description of the advanced funding procedure convincingly demonstrates that the contractors were procurement agents of the United States. Here, it is beyond question that the contractors did not even have to expend any of their own funds for goods or services but were able to disburse monies that at all times belonged to the government. Surely that power to spend government money "gave to the contractors the status of agents of the Government to enter into contracts or to pledge its credit." *Alabama* v. *King & Boozer*, *supra*, 314 U.S. at 13. As the Fourth Circuit correctly observed in *United States* v. *Forst*, *supra*, 569 F.2d at 811, "the key factor in the case was whether the credit of the United States or the contractor was bound by the purchasing agreements." Since Sandia, Zia, and LACI were empowered to write checks on government-owned funds, their power to bind the United States and pledge its credit cannot seriously be questioned.

Contrary to the court of appeals' conclusion, the advanced funding procedure cannot be dismissed as "simply another means of reimbursement devised by accountants * * *" (Pet. App. 23a). There is a considerable difference between the case where the contractor expends its own funds and must await reimbursement by the government and the case in which the contractor is empowered to draw directly on the funds of the government. While the former case may not be inconsistent with an agency relationship (as *Kern-Limerick* itself demonstrates), it

is at least clear that in such a case the contractor must rely upon the government's ratification of its actions in order to obtain reimbursement for its outlays. Here, the contractors did not even take that risk, for they disbursed government funds to the vendors and to their employees in the first instance. In every sense of the word, the contractors here acted on behalf of the government vis-a-vis the vendors. If the contractor receiving after-the-fact reimbursement in *Kern-Limerick* was deemed to be an agent of the United States so that sales to it were thereby immune from state taxes, the case for immunity here follows a fortiori because the contractors had the additional authority to disburse government funds and pledge the credit of the United States.

Although the court of appeals acknowledged that the advanced funding procedure created "appearances" of agency status for the contractor (Pet. App. 22a), it resisted the conclusion that the contractors were immune from state taxes, relying on the fact that "[a]t most, the contractor may pledge to the limit of its letter of credit" (*id.* at 22a-23a). As the court reasoned, "[s]een in this light, Sandia, Zia and LACI are like numerous businesses which deal under letters of credit from banks and other sureties" (*id.* at 23a).

But the conclusion that the contractors' purchases and disbursements are subject to state gross receipts taxes does not follow from the fact that their letters of credit are limited in amount. The claim of immunity here is only coextensive with the contractors' authority to act on behalf of the government. The fact that their authority, like the authority of many agents, is limited in dollar amounts does not refute the argument that they act as agents of the government when acting within the scope of their authority.

Simply because there is some limit upon an agent's authority does not cast doubt upon the existence of the agency relationship itself.

(2) *Contract Modifications.* Finally, if any doubt remains as to the procurement agent status of the contractors in this case, it is dispelled by the modifications to the contracts made as of July 1, 1977. The typical modification recited in pertinent part as follows (J.A. 49-52): [13]

> WHEREAS, the parties recognize that under this contract and the long-standing relationship and practice of the parties hereunder Sandia Corporation acts and has acted as an agent for and on behalf of ERDA [Energy Research Development Administration—now part of DOE] and the Commission for certain purposes; and
>
> WHEREAS, for the benefit of persons who are not parties and not familiar with the contractual relationships and practices hereunder, the parties desire to have the contract reflect the long-standing agency status and authority of Sandia Corporation for certain purposes; * * *
>
> * * * * *
>
> The following article is added to the contract as Article XX:
>
> *Article XX. Status and Authority of Sandia Corporation as an Agent of ERDA*
>
> Under the provisions of this contract, Sandia Corporation has performed and will continue to perform as a management contractor of ERDA. On the basis of certain provisions of this contract and the long-standing relationship and practice of the parties hereunder, it is recog-

[13] There are comparable modifications of the contracts with Zia (J.A. 54-57) and LACI (*id.* at 58-61).

nized that Sandia Corporation acts as an agent for and on behalf of ERDA for certain purposes. Particular provisions and features of the contractual relationship which establish the agency status of Sandia Corporation and the extent of the status and authority thereby created include, but are not limited to, the following:

1. Only ERDA funds are to be used in the performance of this contract by Sandia Corporation, and no funds of Sandia Corporation or of Western [Electric] are required. The funds of ERDA made available for performance of this contract pursuant to the provisions hereof and pursuant to any special bank accounts established hereunder, including all revenues received by Sandia Corporation in the conduct of operations hereunder, are and shall remain the funds of ERDA until expended and shall not at any time become the funds of Sandia Corporation or Western. Sandia Corporation acts as agent for and on behalf of ERDA in disbursing ERDA funds, by the drawing of checks on special bank accounts or by any other method approved by ERDA, for the payment and satisfaction of all obligations properly incurred by Sandia on behalf of ERDA in accordance with the provisions of this contract.

* * * * *

2. * * * Sandia Corporation in the performance of this contract acts as the agent of ERDA in the purchase, lease, or other acquisition, and in the management, maintenance, protection, safeguarding, sale, and disposition of all property of any kind whatsoever, real or personal, used in the performance of this contract.

* * * * *

> 4. ERDA considers all obligations properly incurred in accordance with the provisions of this contract to be ERDA obligations from their inception. Sandia Corporation acts as agent of ERDA in making appropriate payments to all obligees and is responsible for taking any and all other actions as may be necessary for appropriate and timely discharge of all such ERDA obligations. The purpose of this article is to recognize and express existing relationships. This article shall not be construed to modify any other provisions of the contract nor shall it create rights or obligations not otherwise provided for in the contract.

In holding that Zia, Sandia, and LACI were not tax-immune procurement agents of the United States, the court of appeals rejected the plain meaning of the foregoing contract modifications on the ground that they conclude with the caveat that they "shall not be construed to modify any other provisions of the contract * * * nor shall [they] create rights or obligations not otherwise provided for in the contract" (J.A. 57). As the court stated, "[b]ecause we are convinced that, as a matter of law, the provisions of the contracts before the amendments did not establish agency status, we need not be swayed by amendments which make no changes" (Pet. App. 26a).

But the court of appeals' analysis misses the point of the contract modifications. They were not designed to alter the substantive relationship provided by the contracts but to confirm the "agency status of the Contractor * * * [to] include * * * the following: * * * The Contractor acts as agent for and on behalf of ERDA in disbursing ERDA funds * * * [and] the Contractor is authorized to pledge the

credit of the United States in any and all such [purchasing, leasing, and acquisitions of property] transactions, contracts, and other arrangements" (J.A. 55-56). Indeed, in quoting from the clause that stated that the modifications were not to alter any other provisions of the contract, the court omitted the phrase "including, but not limited to, the article entitled Allowable Costs, Base Fee and Award Fee)" (*id.* at 57). See also *id.* at 61. Cf. *id.* at 52. The omitted phrase shows that in confirming the contractors' status as procurement agents, the parties did not intend to modify any other substantive rights and obligations under the contracts.[14]

2. At all events, the fact "that the agency terminology does not appear uniformly in all the documents relating to the contracts" (Pet. App. 26a) does not effectively distinguish this case from *Kern-*

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[14] Contrary to the court of appeals' further observations (Pet. App. 26a), the facts that the purchase orders refer to the contractors as the "Buyer" (see J.A. 120) and that Sandia's contract requires it to make purchase orders in its own name (see J.A. 36-37) does not support its conclusion that the contractors were not procurement agents. As we have pointed out (see page 31, *supra*), the contractors' checks or their identities fully advised third parties that they were dealing with procurement agents for the government. Moreover, the same purchase order (cited by the court of appeals) that refers to the contractor as the "Buyer" modifies that term with the phrase "in the performance of the prime contract * * *," *i.e.*, pursuant to which it acts as a procurement agent (J.A. 120). Finally, while the Sandia contract requires Sandia to make purchase orders in its own name, it further requires that "Sandia Corporation shall insert in such purchase orders * * * such clauses respecting Government property * * * as the Commission may require * * * [and] shall observe the Commission's requirements respecting acquisition and use of property" (*id.* at 37).

Limerick, as the court of appeals apparently believed. Much the same argument was advanced by the State of Tennessee and rejected by the Tennessee Supreme Court in *United States* v. *Boyd*, 211 Tenn. 139, 363 S.W.2d 193 (1962), aff'd on another issue, 378 U.S. 39 (1964). There, the Tennessee court held that the contractor under the identical standard DOE management contract with advanced funding was immune from state sales taxes. In response to the argument that the contract did not in all respects employ the identical *Kern-Limerick* terminology of "agency," the court stated, in terms that are equally appropriate here (211 Tenn. at 155; 363 S.W.2d at 200):[18]

> The mere placing of terms such as agent or independent contractor in the contract does not make them such in law. The surrounding facts and circumstances determine the relationship.
>
> * * * It appears from the contract and from the actions of the parties that the relationship of agency in so far as the purchase of materials are [sic] concerned when accomplished in ac-

[18] The aspect of *Boyd* upon which we rely is the sales tax portion of the case that was considered by the Tennessee Supreme Court, which the State did not appeal to this Court (see 378 U.S. at 43 n.5). The issue before this Court was the constitutionality of the state use tax as applied to the contractor. This Court affirmed the Tennessee Supreme Court's holding that the State could impose a tax on a government contractor on the use of tangible personal property for private gain in the performance of a contract because the contractor's property had not been "so incorporated into the government structure as to become instrumentalities of the United States and thus enjoy governmental immunity" (*id.* at 48). However, as we have pointed out (pages 23-25, *supra*), the Tennessee use tax involved in *Boyd* was not a compensating use tax of the type involved here. The decision of this Court in *Boyd* therefore has no bearing on this case.

> cordance with the contract bring them within the holding of Kern-Limerick and under that case the A.E.C. is the purchaser. Therefore, the Sales Tax would be a direct tax upon the Government and is invalid under the doctrine of implied immunity, and we so hold.

To the same effect is *United States* v. *Nevada Tax Commission*, 291 F. Supp. 530 (D. Nev. 1968), aff'd, 439 F.2d 435 (9th Cir. 1971), a case that the court of appeals here conspicuously ignored, and which likewise cannot be squared with the decision below. There, as here, the state sought to impose its sales and compensating use tax upon a government contractor's purchase and use of tangible personal property under the identical standard DOE contract. In accordance with the advanced funding procedure, the contractor purchased the property with government-owned funds, and title to the property vested immediately in the government. Relying on *Kern-Limerick*, the district court upheld the contractor's claim that the sales were immune from a comparable Nevada sales and compensating use tax modeled after a California statute. As the court there concluded, "all sales by retailers to [the contractor] under this contract, the purchase price being paid by the Government and title passing immediately to the Government, are sales to the United States immune from the Nevada Sales Tax" (291 F. Supp. at 533). The Ninth Circuit affirmed "[f]or the reasons stated in the reported decision of the district court" (439 F.2d at 441).[16]

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[16] See also *United States* v. *Bureau of Revenue*, 87 N.M. 164, 166-170, 531 P.2d 212, 215-218 (Hernandez, J., concurring) (1975). There, the concurring opinion concluded

In sum, we submit that, taken as a whole, the contracts and their implementation, under the advanced funding procedure employed for the management of the government's atomic facilities, demonstrate the existence of an agency relationship for procurement purposes between Zia, Sandia, and LACI, and the United States. The 1977 contracts modifications simply confirm what had always been the case.[17] Although the court of appeals stated that

---

that the contractors were immune from the gross receipts tax because they did not "receive" the advanced funds within the meaning of the statute (87 N.M. at 167). As for the compensating use tax, the concurring judge determined, on the authority of *United States* v. *Nevada Tax Commission*, *supra*, that the tax was not applicable because the purchased property at all times belonged to the government and was therefore exempt under the statute (87 N.M. at 170).

[17] At the outset, there was no need for the parties to confirm the agency relationship because the State had previously recognized that the contractors were procurement agents "for a period of about twenty years before these modifications were made" (Pet. App. 6a). See also J.A. 223-230. During this period, the State did not seek to impose taxes either on the advanced funds or on the sales to the government through the contractors.

Nor is there any basis for the State's argument in the courts below that without congressional authorization, the government had no authority to modify the contracts for the purpose of achieving tax immunity. As the district court succinctly stated, "This argument is disposed of by the conclusion that the Government and the contractors herein maintained an agency relationship for procurement purposes during the years of operation prior to the contract modifications, and have continued to do so to the present. They were not taxable before the modifications, because such modifications merely made the relationship more express, but did not change the agency relationship which had been in operation for three decades, and which had been recognized as such by the Bureau [of Revenue]" (Pet. App. 6a).

it was "highly skeptical of the sporadic addition of 'magic words' to a contract in an attempt to avoid state taxation" (Pet. App. 26a), this Court in *Kern-Limerick* specified, to the contrary, that "the form of contracts, when governmental immunity is not waived by Congress, may determine the effect of state taxation on federal agencies, for decisions consistently prohibit taxes levied on the property or purchases of the Government itself" (347 U.S. at 122-123; footnotes omitted). The explicit terms of these contracts establishes the governmental immunity of the contractors' purchases for the United States from state sales and use taxes.

CONCLUSION

The judgment of the court of appeals should be reversed.

Respectfully submitted.

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SEPTEMBER 1981

APPENDIX

N.M. Stat. Ann. 1953 (Supp. 1975):

§ 72-16A-3. *Definitions.*—As used in the Gross Receipts and Compensating Tax Act [72-16A-1 to 72-16A-19]:

* * * * *

B. "buying" or "selling" means any transfer of property for consideration or any performance of service for consideration;

* * * * *

E. "engaging in business" means carrying on or causing to be carried on any activity with the purpose of direct or indirect benefit;

F. "gross receipts" means the total amount of money or the value of other consideration, received from selling property in New Mexico, from leasing property employed in New Mexico or from performing services in New Mexico, and includes any receipts from sales of tangible personal property handled on consignment but excludes cash discounts allowed and taken, New Mexico gross receipts tax payable on transactions for the reporting period and taxes imposed pursuant to the provisions of the County Sales Tax Act [13-2-30 to 13-2-35], the County Gross Receipts Tax Act [15-55-1 to 15-55-15] or the Municipal Gross Receipts Tax Act [14-61-1 to 14-61-8] which are payable on transactions for the reporting period and any type of time-price differential.

In an exchange in which the money or other consideration received does not rep-

resent the value of the property or service exchanged, "gross receipts" means the reasonable value of the property or service exchanged.

* * * * *

"Gross receipts," for the purposes of the business of buying, selling or promoting the purchase, sale or leasing, as factor, agent or broker, on a commission or fee basis, of any property, service, stock, bond or security, includes only the total commissions or fees derived from the business;

* * * * *

L. "use" or "using" includes use, consumption or storage other than storage for subsequent sale in the ordinary course of business or for use solely outside this state.

§ 72-16A-4. *Imposition and rate of tax— Denomination as "gross receipts tax."*—A. For the privilege of engaging in business, an excise tax equal to four per cent [4%] of gross receipts is imposed on any person engaging in business in New Mexico.

B. The tax imposed by this section shall be referred to as the "gross receipts tax."

§ 72.16A-7. *Imposition and rate of tax—Denomination as "compensating tax."*—A. For the privilege of using property in New Mexico, there is imposed on the person using property an excise tax equal to four per cent [4%] of the value, at the time of acquisition or of introduction into the state, whichever is later, or of conversion to use by the manufacturer of property that was:

(1) manufactured by the person using the property in the state;

(2) acquired outside this state as the result of a transaction that would have been subject to the gross receipts tax had it occurred within this state; or

(3) acquired as the result of a transaction which was not initially subject to the compensating tax imposed by subsection A(2) of this section of the gross receipts tax but which transaction, because of the buyer's subsequent use of the property, should have been subject to the compensating tax imposed by subsection A(2) of this section or the gross receipts tax.

B. For the privilege of using services rendered in New Mexico, there is imposed on the person using such services an excise tax equal to four per cent [4%] of the value of the services at the time they were rendered. The services, to be taxable under this subsection, must have been rendered as the result of a transaction which was not initially subject to the gross receipts tax but which transaction, because of the buyer's subsequent use of the services, should have been subject to the gross receipts tax.

C. The tax imposed by this section shall be referred to as the "compensating tax."

* * * * *

§ 72-16A-12. *Exemptions.*—Exempted from the gross receipts or compensating tax are those receipts or uses exempted in sections 72-16A-12.1 through 72-16A-12.30 NMSA 1953.

§ 72-16A-12.1. *Exemption—Gross receipts tax —Governmental agencies.*—Exempted from the

gross receipts tax are the receipts of the United States or any agency or instrumentality thereof or the state of New Mexico or any political subdivision thereof.

* * * * *

§ 72-16A-12.2. *Exemption—Compensating tax —Governmental agencies—Indians.*—Exempted from the compensating tax is the use of property by the United States or any agency or instrumentality thereof or the state of New Mexico or any political subdivision thereof.

* * * * *

§ 72-16A-14. *Deductions.*—In computing the gross receipts tax due, only those receipts specified in sections 72-16A-14.1 through 72-16A-14.32 NMSA 1953 may be deducted. Receipts, whether specified once or several times in sections 72-16A-14.1 through 72-16A-14.32 NMSA 1953, may be deducted only once from gross receipts.

* * * * *

§ 72.16A-14.9. *Deduction—Gross receipts tax—Sales to governmental agencies.*—Receipts from selling tangible personal property, other than nonfissionable metalliferous mineral ore, to the United States or any agency or instrumentality thereof or the state of New Mexico or any political subdivision thereof may be deducted from gross receipts. Receipts from selling tangible personal property, other than nonfissionable metalliferous mineral ore, to the governing body of any Indian tribe or Indian pueblo for use on Indian reservations or pueblo grants, may be deducted from gross receipts.

* * * * *

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No. 80-702

IN THE

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October Term, 1980

UNITED STATES OF AMERICA, *Petitioner,*

v.

STATE OF NEW MEXICO, *et al., Respondents.*

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE TENTH CIRCUIT

BRIEF OF THE STATE OF NEW MEXICO

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QUESTIONS PRESENTED

1. Whether three private corporate contractors performing contracts for the United States Atomic Energy Commission ("AEC") and its successors are subject to the New Mexico gross receipts and compensating taxes (§§72-16A-1, *et seq.*, N.M.S.A. 1953) on funds received under their contracts to pay salaries and related costs of their own employees, their own award fees, and obligations to third party suppliers from whom they have ordered in their own names.

2. Whether reliance by three private corporate contractors on an "advanced funding" arrangement pursuant to 41 U.S.C. §255, §4(c)(2) of the Atomic Energy Act of 1946, now codified at 42 U.S.C. §2061(b), and 31 C.F.R. Part 205 (1976) to finance their performance of contract work for the Atomic Energy Commission, renders such contractors federal agents exempt from the New Mexico gross receipts tax on such funds, where the funds are used to meet the contractors' obligations, not those of the federal government.

3. Whether, in the absence of Congressional authorization, agency-creating clauses inserted in contracts with three private corporate contractors performing work for the Atomic Energy Commission, insulate them from the New Mexico gross receipts and compensating taxes.

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BRIEF OF THE STATE OF NEW MEXICO

OPINIONS BELOW

The opinion of the district court (Pet. App. 1a-10a) is reported at 455 F.Supp. 993. The opinion of the court of appeals (Pet. App. 11a-28a) is reported at 624 F.2d 111.

JURISDICTION

The jurisdictional requisites are adequately set forth in the United States' Brief, 1.

STATUTES INVOLVED

Additional parts of New Mexico's Gross Receipts and Compensating Tax Act, N.M. Stat. Ann. 1953, §§72-16A-2, 72-16A-3K [(as amended) (1978 Supp.)], 72-16A-12.17 and 72-16A-14.9 [(as amended) (1978 Supp.)], are set forth in App. A, *infra.* Also set forth are 41 U.S.C. §255, §4(c)(2) of the Atomic Energy Act of 1946, codified at 42 U.S.C. §2061, and 31 C.F.R. Part 205 (1976), as Appendices B, C and D, *infra.*

STATEMENT OF THE CASE

This case raises the issue of why three "standard" private contractors working for the Atomic Energy Commission should be deemed "procurement agents," immune from the New Mexico gross receipts and compensating taxes, U.S. Brief, 3. It is conceded that the contractors, all subsidiaries of large corporations, do not meet the tests of a federal instrumentality, U.S. Brief, 2, 3; J.A. 201. It is conceded that the contractors "may be" independent contractors in "directing the details of day-to-day research . . . and the hiring and direct supervision of employees," J.A. 197. It is conceded that the contractors' 7,400 employees, whose salaries and related benefits account for 58% of the contractors' costs, are not employees of the federal government which disclaims liability for their torts, J.A. 200, R.IV, Interrogs. 36, 52, Aug. 31, Oct. 15, 1976. In dealing with third-party suppliers, the contractors are required to order in their own names, J.A. 36-37. Their purchase forms specifically identify them as the "Buyer," as distinguished from the government itself, J.A. 120.

The United States repeatedly stresses the "standard" content of the New Mexico contracts as evidence that the contractors

are tax-immune "procurement agents," U.S. Brief, 3, 15, 16, 17, 26-28, 39, 40. The underlying premise is refuted by the United States' own witness who agrees that "[t]he contract document is *not* a standard form except for the necessary boiler plate. It is tailored in general terms to the particular programs and relationships of the parties," R.VI, Carretta depo., 16, emphasis added. The "standard" contract feature on which the United States bases its entire case is the financing of the contractors' operations through an "advanced funding" arrangement by which the contractors draw funds from a federal reserve bank, pursuant to a letter of credit administered by the Treasury Department, to cover checks previously issued to their obligees, U.S. Brief, 4. The United States concedes that it is the *contractors* who pay their own employees and suppliers, *id.* The United States acknowledges that the advanced funding arrangement places funds at the *contractors'* disposal; it does not extend to the contractors' obligees, *id.*

Advanced funding has been used by AEC and its successors for some thirty years as an expedient method to "speed up reimbursement" of "cost-reimbursed operating contractors," J.A. 189, 204. It is widely used throughout the government; the AEC contractors number a mere one hundred and sixty-five out of 10,369 current recipients, R.VI, McGrath depo., 9.

On July 1, 1977, two years after this case commenced, the United States and the contractors entered into modifications which stated that each contractor "acts as an agent," J.A. 50, 55, 59, while disclaiming any intent to "formally and directly designat[e] the contractors as agents," J.A. 64. The modifications further state that they shall "not be construed" to "create rights or obligations not otherwise provided for in the contract," J.A. 52, 57, 61.

Sandia Corporation receives no fee for its work. However, its parent, Western Electric, receives royalty-free licenses from

Sandia's work, salary reimbursements totalling $312,000 in a sample year and additional payments for audit services and supervision, J.A. 35, 40-42; R.IV, Interrog. 40, Aug. 31, 1976. Western Electric also made over six billion dollars of profit-making sales to the United States between 1966 and 1975, R.IV, Interrog. 44, ex. 2, June 22, 1977.

The characterization of the New Mexico gross receipts tax as falling upon persons "engaged in the construction business or in performing services of a professional, technical, or scientific nature," U.S. Brief, 5, is not sufficiently descriptive. In pertinent part, the tax is upon the "privilege of engaging in business", §72-16A-4, N.M.S.A. 1953. "Engaging in business" means "carrying on or causing to be carried on any activity with the purpose of direct or indirect benefit", §72-16A-3(E). The tax is levied upon the "gross receipts" of a person engaging in business, defined as "the total amount of money or the value of other consideration, received from selling property in New Mexico . . . or from performing services in New Mexico . . .", §72-16A-3(F). The "compensating tax" is levied on the "privilege of using property in New Mexico" and, in pertinent part, is levied on property "acquired outside this state as the result of a transaction that would have been subject to the gross receipts tax had it occurred within this state", §72-16A-7.

Except for a limited number of exempted entities or transactions, the gross receipts tax falls on virtually everyone doing business in the state. As distinguished from many sales taxes, it falls on receipts both from selling goods and performing services, §72-16A-3(F). Thus, doctors, lawyers, consultants and contractors pay it, along with retailers and other merchants. As conceded by the United States, its statutory legal incidence falls on the vendor of goods and services, not the customer, U.S. Brief, 25. Thus, the fact that the United States is the customer of a contractor does not bar the tax on the contractor.

The United States characterizes *United States v. Bureau of Revenue*, 87 N.M. 164, 531 P.2d 212 (Ct.App. 1975), as concerning the gross receipts tax, the same tax at issue here, U.S. Brief, 6. In fact, that case concerned the Emergency School Tax, predecessor to the gross receipts tax, which was repealed in 1967. This error should be corrected since it bolsters the United States' later contention that it failed to modify its contracts before 1977 because "the State had previously recognized that the contractors were procurement agents", U.S. Brief, 41, n. 17.

SUMMARY OF ARGUMENT

In *James v. Dravo Contracting Company*, 302 U.S. 134 (1937), this Court upheld the application of a non-discriminatory state gross receipts tax to the receipts of a federal contractor. So long as the legal incidence of the tax fell on the contractor, the fact that the economic burden passed to the United States did not bar the tax. In the present case, the court of appeals upheld the application of just such a gross receipts tax as was approved in *James v. Dravo* to the receipts of three Atomic Energy Commission contractors performing under contracts in New Mexico.

The United States contends that the three contractors are immune from the New Mexico tax by virtue of being federal "procurement agents", based on *Kern-Limerick, Inc. v. Scurlock*, 347 U.S. 110 (1954). This case held that federal contractors were insulated from state sales taxes in their dealings with suppliers through contracts and purchase orders explicitly stating that "The Contractor shall act as the purchasing agent of the Government" and that "The Government shall be obligated to the Vendor for the purchase price", 347 U.S. at 113, n. 2, 119. The United States' dilemma in applying *Kern-Limerick* to the present case is that fifty-eight percent of the contractors' gross

receipts went to meet their own payrolls, employee benefit packages and internal costs, R.IV, Interrogs. 36, 52, Aug. 31 and Oct. 15, 1976, rather than obligations to suppliers. The United States concedes that the contractors' employees are not employees of the United States and denies any tort liability arising from their activities, J.A. 200. It further concedes that the contractors do not meet the tests of federal instrumentalities, J.A. 201, and "may be . . . 'independent contractor[s]', rather than . . . 'servant[s]' for . . . directing the details of day-to-day research or maintenance operations and the hiring and direct supervision of employees. . .", J.A. 197. Given these concessions, it is clear that the contractors do not function as "procurement agents" in dealing with their own employees and are taxable on the receipts reflecting these costs.

The remainder of the contractors' receipts relate to transactions with suppliers, but the contractors do not function as procurement agents. Their contracts and purchase orders are devoid of language designating them as agents or manifesting an equivalent intent, R.IV, Interrogs. 11, 12, Aug. 31, 1976, Feb. 7, 1977. To the contrary, the contract of Sandia, for example, requires that "All purchase orders, subcontracts and other commitments shall be made in the name of Sandia Corporation. . .", J.A. 36-37. Similarly, another contractor's purchase documents specify that the "Buyer" is "THE ZIA COMPANY in the performance of the prime contract W-17-028-ENG-90 with the United States of America and includes any duly authorized representative thereof", J.A. 120, emphasis in the original. The same documents separately define the "Government" to mean only "the United States of America", J.A. 120, differentiating it from the contractors who are the "Buyer[s]".

Conceding that "[t]he agency relationship in *Kern-Limerick* was express" while the purported relationship here must be "implied", R.III, Plaintiff's Opposition to Defendants' Cross Motion For Summary Judgment, 10, the United States hangs its entire case on the fact that the contractors are financed

through an "advanced funding" method. To relieve them of the need to secure private financing, the contractors are authorized to draw funds from a federal reserve bank, pursuant to a letter of credit system administered by the Treasury Department, to cover the checks they issue to obligees, U.S. Brief, 4-5.

The United States would presumably concede that not every contractor paid in advance is a federal procurement agent. Advanced funding is simply a method to "speed up reimbursement" of AEC's "cost-reimbursed operating contractors", J.A. 189, 204. Although their funds are advanced, the AEC contractors are required to submit an annual voucher which is subject to a "reimbursement audit" to "verify the contractors' net expenditures", J.A. 20, 191. Advanced funding is not unique to Atomic Energy Commission contractors which number a mere 165 out of the 10,369 current recipients, R.VI, McGrath depo., 9. The majority of recipients could not possibly be agents of the federal government. They include "States and local governments, educational institutions. . ." and other organizations "outside the Federal Government", 31 C.F.R. §§205.1, 205.2 (1976). Advanced funding is intended to "enable a recipient organization to obtain cash from Treasury promptly. . ." based upon "its own determination" of how much is needed "for its disbursements", *id.*, §205.5.

The mechanics of advanced funding do not accord a supplier a claim directly against the United States. At no time is a third party able to draw directly on a federal reserve bank against a contractor's letter of credit, R.VI, McGrath depo., 21-22. Funds are drawn into the contractors' local accounts only if, and only after, the contractors have issued checks to their obligees, J.A. 109-110. If no drawdown is made, there is no fund for an unpaid supplier to go against. The great significance attributed by the United States to its ownership of the funds in these accounts turns on preservation of a lien, not creation of an agency relationship. The general statute authorizing advanced

funding, 41 U.S.C. §255(c), requires adequate security which "may be in the form of a lien in favor of the Government . . . on the balance in an account in which such payments are deposited". This lien concept is evidenced in the AEC contractors' agreements with their local banks and the United States which provide that title to the funds is retained by the United States "to secure the return of all advances made to the Contractor", J.A. 85, 87. Having reserved a lien for itself, the United States has clearly not exposed the funds to claims by unpaid suppliers.

The issue is not whose funds are being used but rather whose obligations are being satisfied. So long as the contractors' employees are not federal employees and so long as purchase documents identify the contractors as the buyers, the advanced funds satisfy the contractors' obligations and are taxable gross receipts to them. The United States' obligation to provide funds runs only to the contractors themselves. If advanced funding is coextensive with agency, then the 162 similarly-financed contractors within the Atomic Energy Commission are agents, as are the 10,000 recipients outside the federal government. The United States repeatedly emphasizes the "standard" nature of the New Mexico contracts, U.S. Brief, 3, 15-17, 26-28, 39, 40, asserting that it is advanced funding, not some unique designation of the New Mexico contractors, that makes them agents. This stands *Kern-Limerick* on its head.

Two years after this case commenced, the United States and the contractors entered into contract modifications effective July 1, 1977, J.A. 49, 54, 58. As the United States put it, "anticipated issues in the litigation were the motivating factor", Plaintiff's Opposition to Defendants' Motion to Compel Discovery, 3, namely, "to save $10 million per year", R.III, Defendants' Cross-Motion, ex. 11. Their promulgation does nothing but evidence AEC's own perception of how weak its case was up to that point.

While the modifications provide that each contractor "acts as an agent" for the AEC, J.A. 50, 55, 59, it is conceded that this language does not "formally and directly designat[e] the contractors as agents", J.A. 64. Similarly, although the modifications state that each contractor "is authorized to pledge the credit of the United States", J.A. 51-52, 56, 60, it is conceded that "[t]he word 'is' was not intended to imply that these are words of present authorization", J.A. 64. These qualifications render the modifications a wistful set of arguments as to why advanced funding "establish[es]" an agency relationship, J.A. 50, 55, 59, not a legally operative designation of status. The modifications do not strengthen the United States' assertions regarding advanced funding, they only summarize them.

The fact that Sandia Corporation receives no fee under its cost contract does not exempt it from the New Mexico tax. In *United States v. Boyd,* 378 U.S. 39 (1964), this Court distinguished the use tax exemption accorded a no-fee contractor in *Livingston v. United States,* 364 U.S. 281 (1960), (*per curiam*), *aff'g* 179 F.Supp. 9 (E.D.S.C. 1959), based on the "factual determination that du Pont received no benefits from the contract", 378 U.S. 45, n. 6. The United States minimizes the impact of *Livingston* as applied to Sandia in this case, U.S. Brief, 22-26, and New Mexico concurs, albeit for different reasons. While a no-fee contract might negate the "separable beneficial and taxable use" necessary for use tax liability, *Livingston, supra,* at 22, the same is not true of a tax on receipts relating to a contractor's obligations to its own employees and suppliers. Furthermore, Sandia and its profit-making parent, also a party to this contract, received $312,000 in salary reimbursements, royalty-free licenses and additional payments for audit services and supervision, J.A. 35, 40-42, R.IV., Interrog. 40, Aug. 31, 1976. AEC's own regulations, making receipt of a fee a matter of negotiation, J.A. 211, indicate

no intent that a no-fee contract is indicative of an agency relationship.

Besides *James v. Dravo Contracting Company, supra,* the controlling case here is clearly not *Kern-Limerick* but *United States v. Boyd, supra,* in which this Court held that run-of-the-mill AEC management contractors are neither federal agents nor instrumentalities although they are financed with "government funds" and are relieved of all risk by their cost-plus contracts. Although *Boyd* involved a use tax, this Court's refusal to read an agency relationship into standard contract clauses transcends the particular tax at issue and is dispositive of the present case. While the United States cannot prevail under *Kern-Limerick,* New Mexico urges that this Court abandon this judicially-created exception to the general application of non-discriminatory state taxes to federal contractors. Absent a definitive expression from Congress that federal contractors should escape state taxation, the practice of selectively immunizing contractors through contractual manipulation by the Executive Branch is unjustified. As this Court recently held in a commerce clause context, "[i]t would be strange indeed if the legality of a tax could be made to depend on the vagaries of the terms of contracts", *Commonwealth Edison Co. v. Montana,* 49 U.S.L.W. 4957, 4960, n.8 (1981).

I. THE CONTRACTORS HERE ARE NOT FEDERAL PROCUREMENT AGENTS. THEY ARE LIABLE FOR THE NEW MEXICO GROSS RECEIPTS AND COMPENSATING TAXES ON THE FUNDS USED TO PAY THEIR EMPLOYEES AND SUPPLIERS.

In *James v. Dravo Contracting Company,* 302 U.S. 134 (1937), this Court upheld the application of a non-discriminatory state gross receipts tax to the receipts of a federal contractor. So long as the legal incidence of the tax fell on the contractor, the fact that the economic burden passed to the United States

did not bar the tax. In the present case, the court of appeals upheld the application of just such a gross receipts tax as was approved in *James v. Dravo* to the receipts of three Atomic Energy Commission[1] contractors performing under contracts in New Mexico. The United States concedes that, absent a finding that these three Atomic Energy Commission contractors are federal agents, "the legal incidence of both the New Mexico gross receipts and compensating use tax is on the contractors", U.S. Brief, 25.

To avoid this result the United States asserts that the three AEC contractors are tax-immune federal "procurement agents", U.S. Brief, i, by virtue of *Kern-Limerick, Inc. v. Scurlock*, 347 U.S. 110 (1954). This case held that federal contractors were insulated from state sales taxes in their dealings with suppliers where their contract and purchase orders rendered the United States the "disclosed purchaser". The contract there provided that "The Contractor shall act as the purchasing agent of the Government" and that "the Government shall be directly liable to the vendors for the purchase price", 347 U.S. 110, 113, n.2. Similarly, the purchase orders sent to third parties stated that "This purchase is made by the Government. The Government shall be obligated to the Vendor for the purchase price. . ." and that "The vendor agrees to make demand or claim for payment of the purchase price from the Government. . .", at 119. As the court of appeals in the present case observed, "under *Kern-Limerick* a federal agency may bring a contractor within the scope of intergovernmental immunity if a decision to create an agency relationship is made in advance of a dispute and is *unequivocally expressed* in all relevant documents," Pet.App. 17a, emphasis added.

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[1] In this brief, the agencies with which the contractors are affiliated are referenced interchangeably as the Atomic Energy Commission ("AEC"), the Energy Research and Development Administration ("ERDA"), and the Department of Energy ("DOE"), as the context requires.

To fit *Kern-Limerick* to a gross receipts tax situation, the United States implicitly argues that, to the extent the contractors acted as "procurement agents" in performing their contractual services, their receipts under their cost-plus contracts[2] are insulated from the New Mexico tax. The United States' immediate dilemma is that fifty-eight percent of the contractors' gross receipts went to meet their own payrolls, employee benefit packages and internal costs, R.IV, Interrogs. 36, 52, Aug.. 31 and Oct. 15, 1976, rather than obligations to suppliers. To come within the *Kern-Limerick* tests, the United States must distort the phrase "procurement agent" to include "procurement" by the contractors of their own employees, U.S. Brief, Question Presented, i; 34. Such a claim is unreasonable on its face. Even a genuine agent, immune from tax on the funds which he handles in transactions on behalf of his principal, would experience taxable receipts on payments from the principal to meet the agent's own staff salaries, internal expenses, and profit, *Westland Corp. v. Commissioner,* 84 N.M. 327, 503 P.2d 151 (Ct. App. 1972).

The contractors collectively employ 7,400 employees, R.IV, Interrogs. 37, 71, ex. 2, Aug. 31, 1976. The tasks which these employees perform are indistinguishable from those of other contractors working for the federal government, R.IV, Interrog. 24, ex. 9, Aug. 31, 1976; Interrog. 65, ex. 8, Oct. 15, 1976. The United States concedes that the three management contractors "may be . . . 'independent contractor[s]', rather than . . . 'servant[s]' for . . . directing the details of day-to-day research or maintenance operations and *the hiring and direct supervision of employees. . .*", J.A. 197, emphasis added. The United States further concedes that contractor employees are not government

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[2] One contractor, Sandia, has a cost contract only, since it receives no fee, U.S. Brief, 2.

employees and denies any tort liability arising from "negligence on the part of contractor employees", J.A. 200.[3] Given these facts and the accompanying concessions, it is the contractors, not the United States, which have the obligation of paying these employees. Any funds received from the United States to meet the contractors' recurring payroll and benefit packages constitute receipts to the contractors of a major cost of conducting their business. The United States also concedes that its contractors, despite their status as "procurement agents", *do* owe gross receipts tax on their contractual fees which are "paid by the contractors to themselves from the special Government bank accounts", R.IV, Interrog. 55, Aug. 31, 1976. Having conceded taxable receipt of their fees, the contractors cannot deny equal receipt of, and benefit from, the funds used to meet their obligations to their employees, with whom they deal independent of any "procurement agent" status.

The remainder of the contractors' receipts relate to transactions with suppliers, but the contractors do not function as procurement agents. Nowhere in Zia, LACI and Sandia's contracts and purchase orders are the contractors designated an "agent",[4] empowered to act "on behalf of" or "for the account

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[3] This conforms to the United States' position in *United States v. Boyd*, 378 U.S. 39 (1964), in which it was "not argued that Carbide's 12,000 men have somehow become employees of the Commission rather than of Carbide", at 47-48.

[4] The United States correctly observes that the Tennessee Supreme Court in *United States v. Boyd*, 211 Tenn. 139, 363 S.W.2d 193 (1962), *aff'd*, 378 U.S. 39 (1964), held that the precise use of the word "agent" is not indispensable to finding an agency relationship, U.S. Brief, 39. The same observation was made in *Livingston v. United States*, 179 F.Supp. 9, 22 (E.D.S.C. 1959), *aff'd per curiam*, 364 U.S. 281 (1960). However, the purchase orders in the latter case specified that purchases were "for the benefit of the United States Government", arguably satisfying the *Kern-*

(Cont. p. 14)

of" the government or to "bind the government in any way," R.IV, Interrogs. 11 and 12, Aug. 13, 1976; Interrogs. 11 and 12 Feb. 7, 1977.[5]

The contracts and purchase orders have much language indicating a contrary intent. Negating any notion that Sandia, for example, may bind the government in contract is the flat provision that, "All purchase orders, subcontracts, and other commitments shall be made in the name of Sandia Corporation . . .", J.A. 36-37, emphasis added. Similar intent is expressed in

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[4] (Cont. from p. 13)

Limerick test of disclosed agency. The purchase orders in the *Boyd* case were equally explicit, see page 21, *infra. United States v. Nevada Tax Commission*, 291 F.Supp. 530 (D.Nev. 1968), *aff'd*, 439 F.2d 435 (9th Cir. 1971) never discusses the significance of omitting the word "agent" although it is cited by the United States for that proposition, U.S. Brief, 40. The district court's determination that the United States was the purchaser there was not appealed to the Ninth Circuit. Indeed, the State of Nevada stipulated on appeal that the United States *was* the purchaser, 439 F.2d at 439. The district court opinion is devoid of the factual development in the present record and should not be controlling here, particularly in view of the United States' position in an earlier tort case that the same contractor was *not* its agent, see page 23, *infra.*

[5] Exceptions are purchases by Sandia and Zia from Defense Supply Centers, as to which requisition forms stating that the contractors are "acting on behalf of and as agent for the U.S. Energy Research and Development Administration with respect to the expenditure of Government funds" are utilized, R.V, Vol. 1, exs. 12-S, 12-AF, Feb. 1, 1977. Forms for purchases pursuant to prices negotiated by the General Services Administration, utilized by Sandia and Zia through 1969, stated that they were authorized to "act as agent for" the Commission, but this language was deleted thereafter, *id.*, compare R.V, Vol. 1, exs. 12-W and 12-Y, and 12-AL and 12-AM. Insertion or deletion of such language was "based upon, and varies according to, the requirements of applicable regulations of GSA [General Services Administration] or other Government agencies responsible for such Government supply sources", R.IV, Interrog. 12, Aug. 31, 1976.

the provision that "Sandia Corporation shall . . . be responsible for determining the kind and quantity of materials to be procured, selection of and negotiations with suppliers, negotiation of price or price basis and other purchase terms and conditions . . .", J.A. 36. Rather than placing the contractors under the United States' direct control, it is provided that "Western [Sandia's parent company] shall be responsible for, and shall supervise, performance by Sandia Corporation of its obligations [relating to personnel practices and procurement]," J.A. 37.

Similar intent is expressed in the contractors' internal Purchasing Instructions, approved by the United States, J.A. 36-37, which admonish employees to "CONSIDER FIRST THE INTERESTS OF SANDIA", to act with "utmost loyalty to Sandia", to be "a money manager for Sandia", to make sure they are "getting the best deal for Sandia" before committing "Sandia Corporation funds" and caution them to avoid "the risk of monetary loss to Sandia", R.III, Defendants' Cross-Motion, ex. 10, emphasis in the original.

The contractors' "Standard Terms and Conditions" accompanying all purchase orders distinguish between the "Government" and the "Buyer" who is placing the order. In the case of Zia, for example, the "Buyer" is not the United States but "THE ZIA COMPANY in the performance of the prime contract W-17-028-ENG-90 with the United States of America and includes any duly authorized representative thereof." J.A. 120, emphasis in the original.

These same Standard Terms and Conditions define "Government" to mean only "the United States of America," J.A. 120, para. 1(d). Clearly, the "Buyer" is the contractor, not the separately-defined "Government". Since the government can compel the inclusion of any clauses it wishes in these purchase

orders, J.A. 36-37, the absence of any indication that the contractors are agents is significant and probative.[6]

The United States identifies four tests of an agency relationship in *Kern-Limerick*, and argues that these contractors satisfy them, U.S. Brief, 29, *et seq.* In fact, they do not. As to "governmental approval of purchases", the United States concedes that the contractors in *Kern-Limerick* required advance approval by the United States of *all* purchases, 347 U.S. at 120, while the contractors here operate with "greater autonomy", U.S. Brief, 31. The United States' identification of "immediate passage of title [to purchases] from the vendor to the government" as a test of agency, U.S. Brief, 29, is incorrect since this Court has

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[6] The contracts provide certain alternative procedures to those commonly employed which, *if exercised,* might arguably make the contractors into federal agents so long as those procedures were utilized. For example, the contractors' purchase orders are potentially ". . .assignable by Buyer to the Government or its designee," J.A. 138. Similarly, "ERDA can elect to make payment. . . directly to the obligees [for] obligations properly incurred [by the contractors]", R. II, Plaintiff's Motion, Points and Authorities, 7. Also, contractors could be required to make "such. . . payments on behalf of ERDA as ERDA shall specifically direct," *id.*, 7, or "procure . . . items for the use of the Commission and other Commission contractors as may be required by the Contracting Officer from time to time. . .," J.A. 20.

It can be seen that *if* purchase orders are assigned to the government, *if* the government paid the contractors' suppliers directly, *if* the government directed the contractor to make payments on its behalf and *if* the government told the contractors what to buy, *then* the contractors might indeed be functioning as agents of the government for those activities. *In other states, ERDA has deliberately structured purchases by contractors so that the government paid the suppliers directly, avoiding state taxes,* J.A. 163-173. But Zia, LACI and Sandia *have never performed any activities pursuant to these provisions,* R. IV, Interrogs. 46, 61, 69, 88, 113 and 117, Aug. 31, 1977; Interrogs. 68 and 100, Oct. 15, 1976. If the contractors were intended to be ERDA's agents in purchasing pursuant to the standard procedures, there would be no need for these alternative procedures.

held that "The circumstance that the title to the lumber passed to the Government on delivery does not obligate it to the contractor's vendor. . .", *Alabama v. King & Boozer*, 314 U.S. 1, 13-14 (1941).[7]

The only evidence proffered to satisfy the third test, "specific notice" of an agency relationship, U.S. Brief, 29, are the legends on checks utilized by Zia and LACI since 1975 and by Sandia since 1976, U.S. Brief, 31. These have the phrases "A.E.C. Advanced Funds" or "Advance Funds Accounts" in the printed portions of the checks, J.A. 99-101. Since the Standard Terms and Conditions sent to suppliers already identify the contractors as the "Buyer[s]", J.A. 120, the check legends only notify obligees of the contractors' funding mechanism. When compared to the emphatic language of the *Kern-Limerick* purchase orders, there is no justification for gratuitously reading an agency relationship into the language on the checks. It may be, as the United States contends, that obligees are aware that they are dealing with federal contractors whose funds ultimately come

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[7] Similarly, in *United States v. Boyd, supra*, the fact that "title to all property passes directly from the vendor to the United States", at 41-42, did not hinder this Court's determination that the contractors were not agents. As further evidence of an agency relationship, the United States also identifies provisions that the United States bears the risk of loss, retains control of the disposition of purchases and approves the contractors' property management procedures, U.S. Brief, 20. These provisions are frequently found in the contracts of obvious non-agents and are irrelevant to the determination of the contractors' purported status as agents. In *United States v. Boyd*, the United States had to approve purchases above a certain amount, controlled "large areas of operation", at 42, and relieved the contractors of all risks, at 44. Equivalent clauses are found in Defense Department contracts, which specifically provide that the contractors are *not* agents, reflecting the Defense Department's blanket policy against designating contractors as agents, see *United States v. New Mexico*, 581 F.2d 803, 804-805, 807, 808, n.1 (10th Cir. 1978) and *United States v. Forst*, 442 F.Supp. 920 (W.D.Va. 1977), *aff'd*, 569 F.2d 811 (4th Cir. 1978).

from the United States, U.S. Brief, 32, n.12. But that is true as to every federal contractor, not just those which are agents, and proves nothing. The fact that cost-plus contractors "in a loose and general sense were acting for the Government," is not sufficient to immunize them from state taxes, *Alabama v. King & Boozer*, 314 U.S. 1, 12 (1941). To be bound on a contract, there must be a "disclosed principal" and an "understanding that the principal is a party", Restatement (Second) of Agency, §144. Here, there is neither the disclosure nor the understanding.

The fourth test, "explicit characterization" of the contractors as agents, U.S. Brief, 29, is purportedly satisfied by the contractors' reliance on "advanced funding" to finance their operations, and by certain contract modifications effective July 1, 1977, *id.*, 32, 35. These are analyzed in Sections II and III of this brief. As will be seen, the modifications stop short of being explicit designations of the contractors as agents, J.A. 64, and simply reference the advanced funding arrangement as the proof of the agency relationship. Earlier in this case, the United States conceded that, while "[t]he agency relationship in *Kern-Limerick* was express", the purported relationship here was only "implied", R.III, Plaintiff's Opposition to Defendants' Cross Motion For Summary Judgment, 10. Now, the United States hangs its entire case on the contention that an element of the contractors' operational style, advanced funding, constitutes the sort of express designation of agency approved in *Kern-Limerick*.

The United States' motivation is clear. Having failed to expressly designate its New Mexico contractors, it must claim that their style of operation establishes an agency relationship. To insert *Kern-Limerick* language here and prevail would expose all its undesignated contractors in other states to taxation. Therefore, the United States repeatedly emphasizes the "standard" nature of the New Mexico contracts, U.S. Brief, 3, 15-17, 26-28, 39, 40, asserting that it is advanced funding, not some

unique designation of the New Mexico contractors, that makes them agents. This rationale stands *Kern-Limerick* on its head.

Additionally, this approach cannot avail the United States because this Court has already scrutinized run-of-the-mill AEC management contractors and concluded that they are neither federal agents nor instrumentalities by virtue of their style of operation, *United States v. Boyd*, 378 U.S. 39 (1964). The Tennessee contractors there were obligated to "manage, operate and maintain the Oak Ridge plants", at 41, although having "no investment" in them, at 42. They were "charged with the duty of procuring materials, supplies, equipment and facilities", at 41, paid for their purchases with "government funds", and caused title to their purchases to pass "directly from the vendor to the United States", at 41-42. The Atomic Energy Commission retained "the right to control, direct and supervise the performance of the work", at 42.

Nevertheless, this Court concluded that neither contractor was "so incorporated into the government structure as to become instrumentalities of the United States and thus enjoy governmental immunity", at 48. There was no special immunity arising from work for the Atomic Energy Commission: "In 1953, Congress repealed the statutory immunity for activities and properties of the AEC contained in §9(b) in order to place Atomic Energy Commission contractors on the same footing as other contractors performing work for the Government", at 40.

The Tennessee management contractors receiving advances of "government funds" were simply another species of cost-plus contractor, "a widespread method of contracting with the Government", at 46. Indeed, "[w]hatever limitations there are on entrepreneurial risks derive from the fact that companies perform under cost-plus-fixed-fee contracts", at 46.

This Court, perhaps with *Kern-Limerick v. Scurlock* in mind, recognized that Atomic Energy Commission operations did not

have to be subject to state taxes. In its enabling legislation, ". . . Congress empowered the AEC to choose between performing these undertakings directly, through its own facilities, personnel and staff, and seeking the assistance of private enterprise by means of grants and contracts," at 47. Therefore, "[s]hould the Commission intend to build or operate the plant with its own servants and employees, it is well aware that it may do so and familiar with the ways of doing it. *It chose not to do so here*", at 48, emphasis added.

Reading an agency relationship into the AEC contractors' style of operation must also fail because the AEC itself never intended that the relationship with its management contractors would, without express designation, be that of principal and agent. Asked whether AEC contractors were "more an agent of the Government than . . . a prime contractor for the Defense Department?", an AEC commissioner responded, "*I would not classify the overall relationships as one of 'agency' in the legal sense. . .*[W]e believe that it is close to being an agent *but is not legally so,*" J.A. 175, emphasis added.

The Commission's stated practice has been to specifically designate a contractor as an agent when it wants the contractor to be one. Thus, "the relationship and control [of the Commission over its contractors] is not so close in fact as to constitute a general or specific agency, *except where so expressly stated. . .*", Ramey and Erlewine, *Introduction to the Concept of the "Administrative Contract" in Government Sponsored Research and Development,* 17 Fed. B.J. 354, 358-359 (1957), emphasis added.

Consistent with this policy, the Atomic Energy Commission "has found it advantageous to enter into . . . *contracts expressly designating the contractor as agent*" for community management, purchases from government supply sources and "for the purpose of administering many substantial procurement con-

tracts which were placed directly by the Commission. . ." Testimony of David Shaw, *Hearings Before a Subcomm. of the Comm. on Gov't Operations, 85th Cong., 1st Sess., on S.6,* June 11 and 12, 1957, 66-67, [emphasis added]. See also, J.A. 216-217. Such agency designations were explicit. Thus, an early AEC contract provided "in the operation of the facilities under this contract, and in the procurement of any and all supplies . . . the Contractor shall act as agent for the United States of America. . .", R.III, Defendants' Cross-Motion, ex. 9, 2. Similarly, the AEC approved purchase orders sent to suppliers by another contractor which provided that "this Order is entered into . . . for and on behalf of the Government", and that ". . . nothing herein shall preclude liability of the Government for any payment properly due hereunder. . .", *United States v. Boyd,* 363 S.W.2d 193, 199 (Tenn. 1962).

These examples notwithstanding, explicit designation of agents rarely occurred, J.A. 216. This resulted from what its Assistant General Counsel termed "a continued reluctance to designate AEC contractors expressly as procurement agents", Hiestand and Florsheim, *The AEC Management Contract Concept,* 29 Fed. B. J. 67, 81 (1969).[8] In the same vein a regional attorney noted that "AEC Washington" was "adverse to use of the term ['agent'] in prime contracts" in the mid-1950's, J.A. 181. This "reluctance" stemmed from strong and continuing

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[8] This "reluctance" is somewhat startling because the Atomic Energy Commission has been highly sensitive since its inception to the need to insulate its contractors from state taxes and to the benefits of attributing an agency status to them. This is evidenced in lengthy submissions to Congress on several occasions resisting legislation which would have eliminated agency as a defense to state taxes, or otherwise exposed AEC contractors to additional taxes, R.V, exs. 22-U, 22-V, 22-W, 22-AA and 22 AE. It is further evidenced in sophisticated analyses of the avenues for avoiding state taxes following this Court's decision in *Kern-Limerick, Inc. v. Scurlock* in 1954, R.V, ex. 22-AB.

policy motives. AEC has been concerned since its inception that designating its contractors as agents would force them to follow all the Federal Procurement Regulations, the sort of red tape that the "management contract concept" was meant to avoid. As Commissioner Ramey noted, "[t]he early AECPR's [Atomic Energy Commission Procurement Regulations] contained language which implied that our contractors in their procurements were to be bound by the same regulations as were binding on direct AEC procurement", R.V, Vol. 2, ex. 22M, 5. Similarly, Assistant General Counsel Hiestand wrote that "[t]he designation of management contractors as purchasing agents caused concern in the early days of AEC, based on the argument that a purchase by an agent was subject to the same legal requirements applicable to direct procurement. . . . Although the fears about procurement through an agent-contractor were largely dispelled by the Supreme Court in *Kern-Limerick, Inc. v. Scurlock, there has been a continued reluctance to designate AEC management contractors expressly as procurement agents*", Hiestand and Florsheim, *supra*, 80-81, emphasis added.

This "continued reluctance" was an enduring element of policy as shown by a 1969 exchange between a Congressional committee aide and an AEC commissioner:

Mr. Roback:	But in all these other areas, the fact that a contractor, *not the Government*, is doing the contracting in a large way exempts these agencies legally from all procurement laws and regulations.
Mr. Ramey:	Not from all, but from some.
Mr. Roback:	Not from all, but in a large way, I say.
Mr. Ramey:	Yes; at least, with respect to the procurement statutes.

J.A. 177, emphasis added.

A 1968 AEC report on contractor procurement rejected a proposal to "[c]onsider the contractors as agents of the Government and require that they follow strictly the FPR and AECPR in their procurement activities. . .," J.A. 183-184, [abbreviations refer to the Federal Procurement Regulations and Atomic Energy Commission Procurement Regulations]. Obviously, if the contractors were already agents by virtue of their mere association with AEC, there would be no need to "consider" them as agents by a new policy formulation.

AEC has consciously refrained from designating its contractors as agents to benefit from their freedom in procurement, *precisely the function for which an agency relationship is now claimed to avoid taxes!* But where the designation is deliberately omitted to gain the benefits of non-agent status, a claim that the contractors are procurement agents must fail.[9]

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[9] AEC has additional motivations for consciously omitting agency terminology from its contracts. AEC routinely asserts that the same contractors which it styles "agents" in tax cases are "independent contractors" in tort cases, R. IV, Interrogs. 98 and 99, Aug. 31, 1976; R. IV, Interrogs. 98 and 99, Feb. 7, 1977. This fluid switching of legal positions would be jeopardized if contractors were formally designated as agents. Illustrative of this practice, in a tort case involving the Reynolds Electrical & Engineering Company (REECO) in 1976, "The AEC contend[ed] that the government cannot, under the Tort Claims Act, be held liable for injuries resulting from the negligence of Reeco, *its independent contractor.* . .", *McGarry v. United States,* 549 F.2d 587, 590 (9th Cir. 1976), emphasis added. Two years later, in a tax case involving the same contractor, the United States took a different stance and successfully argued that sales to REECO "are *sales to the United States* immune from the Nevada Sales Tax", *United States v. Nevada Tax Commission,* 291 F.Supp. 530, 533 (D.Nev. 1968), *aff'd,* 439 F.2d 435 (9th Cir. 1971), emphasis added. While ERDA has not had occasion to argue that Zia and LACI in particular are independent contractors, "[p]laintiff admits that it would take such a position, if otherwise appropriate, in the context of a tort claim against the United States, as admitted with respect to management contractors generally. . .", R. IV, Interrog. 98, Feb. 7, 1977.

II. "ADVANCED FUNDING" MEETS THE UNITED STATES' CONTRACTUAL PAYMENT OBLIGATIONS TO THESE CONTRACTORS. IT DOES NOT CREATE AN AGENCY RELATIONSHIP INSULATING THE CONTRACTORS FROM STATE TAXES.

The United States argues that the contractors are paying their obligees with "the federal government's funds", U.S. Brief, i, and that, therefore, they are procurement agents in disbursing these funds, *id.*, 28. Two decisions by this Court point up the error in this reasoning. In the use tax portion of *United States v. Boyd, supra,* this Court found the contractors to be neither agents nor federal instrumentalities although the contractors paid for their purchases "with government funds", at 41-42. After that decision, those contractors had to pay their use tax from these same "government funds", Record at 6, *United States v. Boyd,* 378 U.S. 39, Original Bill, para. VIII. In doing so, the contractors acted, not as disbursement agents of the government, but as taxpayers meeting their own obligations. In contrast, the contractor in *Kern-Limerick, Inc. v. Scurlock* was held an agent although he did *not* receive advanced funding. This does not suggest a "stronger case for immunity" if a contractor receives advanced funding, U.S. Brief, 14; rather, it suggests that *the issue is who bears the obligation, not whose funds are used.*

Presumably, the United States would concede that not every contractor paid in advance automatically becomes an agent of his customer. Many a person commissioning a new house has paid his contractor in advance for precisely the same reasons the United States does so: to avoid financing costs, to permit retention of a contractor having limited access to credit, and to keep better control over expenditures. The customer's obligation to supply funds runs only to the contractor. Although the contrac-

tor is using "the customer's funds", he does so to meet *his own* obligations to his employees, his suppliers and himself. Thus, the issue is not whose funds are being used, but whose obligations are being satisfied. There is no basis for claiming that advanced funding automatically equals an agency relationship, yet that untenable claim is at the heart of the United States' case.

To briefly reiterate points from the preceding section, Zia and LACI (the two contractors receiving fixed fees) concede that they do owe New Mexico gross receipts tax on their fixed fees which "were paid by the contractors to themselves from the special Government bank accounts", U.S. Brief, 6; R.IV, Interrog. 55, Aug. 31, 1976.[10] Despite the uniqueness attributed to these accounts, and the limitations on the contractors' use of the funds deposited in them, it is conceded that these funds *can* become taxable gross receipts of the contractors. With this concession in hand, the funds used to meet the contractors' extensive payrolls and obligations to suppliers must constitute receipts as well. So long as the contractors' employees are not federal employees and so long as purchase documents sent to third parties identify the contractors as the buyers, the advanced funds satisfy the *contractors'* obligations.

The mechanics of advanced funding do not accord a supplier a claim directly against the United States. At no time is a third party given the power to draw directly on a federal reserve bank against a contractor's letter of credit, R.VI, McGrath depo., 21-22. Funds are drawn into the contractors' local accounts

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[10] More accurately, it is the United States which advances an amount equal to the contractors' fees, a computation determined in the first instance by the contractors themselves under the mechanics of the advanced funding arrangement.

only *if*, and only *after*, the contractors have issued checks to their obligees, J.A. 109-110. If no drawdown is made, there is no fund for an unpaid supplier to go against. The great significance attributed by the United States to its "ownership" of the funds in these accounts turns on preservation of a lien, not creation of an agency relationship. The general statute authorizing advanced payments, 41 U.S.C. §255(c) (1981), requires adequate security for advanced funds which "may be in the form of a lien in favor of the Government. . . on the balance in an account in which such payments are deposited". This lien concept is evidenced in the AEC contractors' agreements with their local banks and the United States which provide that the title to the funds retained by the United States is "to secure the return of all advances made to the Contractor", J.A. 85, para. 2; 87, para. 2.[11] A similar agreement applicable to all federal contractors is found at 41 C.F.R. §1-30.414-1 (1980). Having reserved a lien for itself, the United States has clearly not exposed the funds to any claims by unpaid suppliers.

Although the district court found that "[t]he advanced funding scheme is not a system by which the contractors are *reimbursed* for their direct costs under the contract", and therefore concluded that the contractors were "not the same as the typical cost-plus-fixed-fee contractor", Pet.App. 5a, emphasis added, this finding is at variance with the AEC's own long-

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[11] As a practical matter, funds are only drawn into the accounts by the contractors after they have issued checks to specific obligees, R. VI, McGrath depo., 14-15. Under an alternative arrangement, the local bank advances funds to cover the contractors' checks and then draws funds from the federal reserve bank to reimburse itself, *id.*, 15. Under this second arrangement, the funds never enter the "special" bank accounts at all. Even under the first arrangement, the concept of the United States "owning" funds already earmarked for specific obligees has little significance.

established policy in utilizing advanced funds.[12] AEC instituted an "integrated" accounting system shortly after it came into being, J.A. 189. Far from transforming its contractors into agents, its purpose was to "speed up *reimbursement* of contractors", J.A. 204, emphasis added. Central to this new system was the use of "advanced funds", J.A. 190, authorized under §4(c)(2)(B) of the Atomic Energy Act of 1946, now 42 U.S.C. §2061(b) (1981). Their use, subject to later audit, replaced the "customary procedure in the audit of certain contracts . . . resulting in a triple item-by-item voucher check", J.A. 187.

Despite the shift to advanced funding, AEC continued to view its contractors as "cost-reimbursed operating contractors", J.A. 189. The fact that a major contractor's accounts were "integrated" did not relieve it of a later "*reimbursement* audit" performed by the Atomic Energy Commission, J.A. 191, emphasis added. Thus, although the contractor had the use of the advanced funds, after subsequent audit they were credited against the amounts otherwise subject to reimbursement. The cost-reimbursement language in the contracts in the present case is not an anomaly to be disregarded, as the district court found it to be, Pet. App. 5a. Advanced funding is an advantageous way of paying contractors, not of empowering them to pledge the credit of the government.

Advanced funding is not unique to these contractors nor to the Atomic Energy Commission. It is a funding mechanism

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[12] The district court's finding is also at variance with specific contract clauses assuring that all the contractors' costs will be "reimbursed" by the United States, J.A. 31, and constitute their "compensation", J.A. 18, and establishing an elaborate system for periodic audit and approval of the contractors' vouchers submitted subsequent to expenditure of the advanced funds, J.A. 20, U.S. Brief, 30. It also conflicts with the holding in *United States v. Boyd, supra,* that contractors paid with "government funds" are merely a species of cost-plus-fixed-fee contractor, 378 U.S. 39, 46.

administered by the Treasury Department and available to any federal agency having a relationship with a private entity for longer than one year and for more than $250,000, R.VI, McGrath depo., 7-8. All recipients, including the AEC contractors, are governed by the Treasury Regulations appearing at 31 C.F.R. Part 205, *id.*, 6. The AEC contractors number a mere *one hundred and sixty-five out of a total of 10,369 current recipients, id.*, 9. The majority of recipients could not possibly be agents of the federal government. They include "State and local governments, educational institutions, . . ." and other organizations "*outside* the Federal Government. . .", 31 C.F.R. §§205.1, 205.2 (1976), emphasis added. Current recipients in New Mexico include such obvious non-federal-agents as the towns and cities of Red River, Tularosa and Albuquerque, New Mexico Highlands University, and Six Sandoval Indian Pueblos, Inc., R.VI, McGrath depo., exs. A and B.

Included in the record are affidavits from five of these New Mexico holders of federal letters of credit, J.A. 114-119, R.III, Defendants' Cross-Motion, exs. 2-5. They rely exclusively on federal letter of credit funds to finance particular operations or, in some cases, their entire cost of operation. They do not commingle the federal funds with others. They write checks directly on these letter of credit accounts to cover salaries, materials, supplies and services. They draw on the federal reserve bank through their local bank without any prior clearance from the government. In short, they utilize these accounts exactly as the AEC contractors do, yet they clearly are not federal agents, *id.*

Of particular interest is the affidavit from the New Mexico Professional Standards Review Organization, J.A. 114-119. Its banking arrangements include an agreement among the United States, the bank and the Organization, which is virtually identical to the "special" agreements executed by Sandia, Zia and LACI, J.A. 117-119. Lacking any exemption under New Mexico's tax laws, (such as that afforded a "501(c)(3)" organization

under §72-16A-12.17, N.M.S.A. (1953)), the New Mexico Professional Standards Review Organization routinely "*pays. . . New Mexico gross receipts tax on its payments from the Department of Health, Education and Welfare.*" Furthermore, "[t]hese tax payments are allowable costs reimbursed by the federal agency", J.A. 115, emphasis added.

The letters of credit are intended to "enable a recipient organization to obtain cash from Treasury promptly . . ." based upon "*its own determination*" of how much is needed "for its disbursements", 31 C.F.R. §205.5 (1976), emphasis added. Only a designated recipient is empowered to draw on the Treasury, R.VI, McGrath depo., 21. This power cannot be delegated to third parties, *id.*, 21-22. From the Treasury's point of view, the purpose of advanced funding is solely to delay the draw down on the federal treasury as long as possible to increase the "float" on federal funds, *id.*, 13-16. Negating the United States' contention that the funds "do not pass through the contractors", R.II, Plaintiff's Motion, Points and Authorities, 7, is the requirement of semi-annual reports of "cash balances *in the hands* of the recipient organizations. . .", 31 C.F.R. §205.9 (1976), emphasis added.

Thus, advanced funding is simply a standard mechanism, one of several, by which the United States meets its obligations to its contractors. If these Atomic Energy Commission contractors are agents by virtue of advanced funding, then so are the ten thousand recipients outside the federal government and so are the 162 other recipients *within* the AEC, 102 of whom are not even management contractors, compare R.IV, Interrog. 21, ex. 8, Aug. 31, 1976, and R.VI, McGrath depo., 9. If advanced funding is coextensive with agency, virtually every large Atomic Energy Commission contractor would be an agent purely by virtue of its style of operation, a result which Congress apparently meant to avoid in repealing §9(b) of the Atomic Energy Act of 1946 following the decision in *Carson v. Roane-Anderson*

Co., 342 U.S. 232 (1952). These repercussions both within and without the Atomic Energy Commission are so implausible as to mandate the conclusion that advanced funding does not create an agency relationship between the United States and its contractors.

III. THE JULY 1, 1977, CONTRACT AMENDMENTS STOPPED SHORT OF EXPRESSLY DESIGNATING THE CONTRACTORS AS AGENTS. IF THE CONTRACTORS WERE NOT AGENTS BEFORE, THE MODIFICATIONS DID NOT CHANGE THEIR STATUS.

Two years after this case commenced, the United States and the contractors entered into contract modifications effective July 1, 1977, J.A. 49, 54, 58. As the United States put it, "anticipated issues in the litigation were the motivating factor for the modifications", Plaintiff's Opposition to Defendants' Motion to Compel Discovery, Sept. 7, 1977, 3, this issue being "to save $10 million per year", R.III, Defendants' Cross-Motion, ex. 11.[13] More precisely, they were intended to "show that ERDA [AEC's successor] . . . is willing to use the word 'agent' . . . in the contracts themselves", R.III, Plaintiff's Opposition to Defendants' Cross Motion For Summary Judgment, 18.

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[13] The United States suggests that it failed to modify its contracts before 1977 because "the State had previously recognized that the contractors were procurement agents", U.S. Brief, 41, n. 17. As even the United States concedes, it was aware that New Mexico viewed the contractors as taxable as early as 1967, U.S. Brief, 6, eight years before this case commenced. The United States chose to conduct an earlier litigation from 1967 to 1975 without modifying its contracts, but obviously knew that its contractors were at risk, *United States v. Bureau of Revenue*, 87 N.M. 164, 531 P.2d 212 (Ct. App. 1975). The hastily prepared modifications in 1977 did not result from a sudden realization that New Mexico had changed its position but rather from a realization that the United States' case was extremely weak.

These modifications were presumably designed to bring the contracts within the holding of *Kern-Limerick, Inc. v. Scurlock*, 347 U.S. 110, 122-123 (1954) that "the form of contracts, when governmental immunity is not waived by Congress, may determine the effect of state taxation on federal agencies. . .". However, it is one thing to "use the word 'agent' " and another to unreservedly so designate a contractor as contemplated in *Kern-Limerick*. The modifications here are so hedged with qualifications and cautious language that they in no way affect this case.

With slight variations the modifications provide that each contractor "acts as an agent for and on behalf of ERDA for certain purposes", J.A. 50, 55, 59. However, it is conceded that this phrase does not have the effect of "formally and directly designating the contractors as agents for various purposes in the contract modifications," J.A. 64. In fact "[n]o consideration was given by anyone at any time" to such a formal designation, *id.* Similarly, the modifications provide that each contractor "is authorized to pledge the credit of the United States. . .", J.A. 51-52, 56, 60. Again, the United States concedes that "The use of the word 'is' was not intended to imply that these are words of present authorization.", J.A. 64.

This curious drafting resulted in part from AEC's fear that more explicit modifications would "prejudice our case in prior years when such language did not appear" in the contracts, J.A. 62. But in regard to their retroactivity, even AEC officials wondered, ". . .whether execution of the modifications during the course of the litigation really will have the intended effect of convincing the court that the modifications merely 'recognize existing relationships'," R.III, Defendants' Cross-Motion for Summary Judgment, ex. 11. The refusal to affirmatively designate the contractors as agents, the obvious method of compliance with *Kern-Limerick*, also reflects the fear that a victory in New Mexico based on the modifications would expose all

undesignated AEC contractors to taxes in other states. The United States in its brief waivers as to whether the modifications merely "specify" or "characterize" the contractors as agents, U.S. Brief, 5, 32, or affirmatively "designate" them, *id.*, 21, an interpretation which it has already conceded away, J.A. 64.

The conscious refusal to affirmatively designate the contractors as agents renders the modifications a wistful set of arguments as to why advanced funding "establish[es]" an agency relationship, J.A. 50, 55, 59, not a legally operative designation of status.[14] If, for the myriad reasons set out in this brief, advanced funding does not establish an agency relationship, the modifications do not strengthen the United States' contrary assertions; they merely summarize them.

Further nullifying the impact of the modifications is the express provision that they "shall not be construed to modify any other provisions of the contract *nor . . . create rights or obligations not otherwise provided for in the contract*", J.A. 52, 57, 61. This provision was inserted at Sandia's insistence, J.A. 69. It leaves untouched the provisions that all purchase orders shall be made "in the name of Sandia Corporation", J.A. 36-37, and that, in dealing with suppliers, the "Buyer" is "THE ZIA COMPANY", not the United States, J.A. 120. The contractors did not change their purchase orders in any way, Pet. App. 26a, leaving third parties unaware that they are dealing with an "agent". Contrast this omission with the emphatic purchase orders utilized in *Kern-Limerick* and in the sales tax portion of *United States v. Boyd*, 363 S.W.2d at 199.

In the course of negotiating the modifications, Sandia insisted on alteration of an earlier draft so that its employees would not

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[14] It also confirms New Mexico's thesis that AEC has always been extremely reluctant to expressly designate its contractors as agents and has failed to do so here, see pp. 20-23, *supra*.

be specifically designated as "obligees" of ERDA, for fear that this would disrupt its labor relations, J.A. 69-70. So long as the contractors' employees may have no direct claims against the United States, J.A. 197, 200, the contractors' periodic payrolls remain their obligations, not those of the United States.

The power to contract on behalf of ERDA is delegated pursuant to written "management delegations of authority" issuing from the administrator of the agency, R.VI, Carretta depo., 29. Re-delegations are maintained "in writing, locally that is," and "hopefully there were written delegations in the field that got to the name as well as the position", *id.*, 31, 32. It is conceded that the modifications themselves were not formal and direct designations of the contractors to act on behalf of AEC, J.A. 64. There is no evidence of any other written delegation to these contractors. Furthermore, although ERDA's Division of Procurement was advised of the modifications, no official approval of them emanated from that office. Instead, a conscious decision was made that "matters concerning the legal relationships existing between ERDA and its management contractors were matters on which Division of Procurement should defer to the General Counsel, and . . . no response . . . from Division of Procurement was required," R.I, Interrogs. 125-132, 135-136.

ERDA's Albuquerque attorneys decided that they "did not need to ask ERDA Headquarters to 'approve' the modifications", J.A. 77. The General Counsel's office of ERDA in Washington expressed "no objections" to the modifications, R.I, 136, but the modifications themselves did not constitute a present delegation of any powers, J.A. 64. Accordingly, the purported delegation of agency powers to these contractors did not satisfy ERDA's procedures and is invalid.[15] Indeed, AEC tacitly

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[15] It is also unclear whether Congress intended in the Atomic Energy Act of 1946 to authorize delegation of AEC's power to contractually-created agents. Forty-two U.S.C. §2014(a) defines "agency of the United States"

(Cont. p. 34)

concedes that the authority of these contractors to "sign contracts. . . on behalf of ERDA" is not to be found in the procedures granting authority to ERDA's own officials and employees, R.IV, Interrog. 120, Aug. 31, 1976.

If the contractors were not agents before July 1, 1977, the modifications do not change their status. Unless all AEC contractors utilizing advanced funding are automatically federal agents, the modifications in no way support singling out these three contractors.

IV. THE FACT THAT SANDIA CORPORATION PERFORMS ITS CONTRACT WITHOUT RECEIVING A FEE DOES NOT RENDER IT A FEDERAL AGENT.

Zia and LACI are elements of a large conglomerate and receive fees for their work for AEC, R.IV, Interrog. 73, Aug. 31, 1976; J.A. 18, 27. Although Sandia is a for-profit corporation, and a subsidiary of Western Electric Company, its contract specifies

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[15] (Cont. from p. 33)
to include the three branches of government and "any Government agency". In pertinent part, "Government agency" includes "any executive department" and any "independent establishment" or "corporation" which is "wholly or partly owned by the United States of America" and which is "an instrumentality of the United States", 42 U.S.C. §2014(1). The contractors here are concededly not instrumentalities, J.A. 201, and are not wholly or partly owned by the United States, R. IV, Interrog. 8, Aug. 31, 1976. Having specifically defined the criteria of a "Government agency", none of which these contractors satisfy, Congress pre-empted the power to create lesser, contractual, agency relationships. The points at which the term "Government agency" is used in the Act do not shed much light on this issue, see 42 U.S.C. §§2020, 2031, 2064, 2164(d), 2165(c) and 2201(f).

that it receives no fee or profit, J.A. 31. In *United States v. Boyd*, 378 U.S. 39 (1964), this Court distinguished the use tax exemption accorded a no-fee contractor in *United States v. Livingston*, 364 U.S. 281 (1960) (*per curiam*), *aff'g* 179 F.Supp. 9. (E.D.S.C. 1959), based on the "factual determination that du Pont received no benefits from the contract", 378 U.S. at 45, n.6. Following *Boyd*, *Livingston* is relevant to the present case only if a no-fee contract automatically renders Sandia a federal agent. The United States concedes that Sandia does not meet the tests of a federal instrumentality, J.A. 201, and minimizes the impact of *Livingston* as applied to Sandia, U.S. Brief, 22-26.[16] New Mexico concurs, albeit for different reasons. While a no-fee contract might negate the "separable beneficial and taxable use" necessary for use tax liability, *Livingston, supra*, at 22, the same is not true of a tax on receipts relating to a contractor's obligations to its own employees and suppliers.

Du Pont had a much closer relationship with AEC than does Sandia. Du Pont worked "in close collaboration" with, and under the supervision of, two hundred and thirty AEC employees at the site, 179 F.Supp. at 18. Sandia receives little day-to-day supervision from AEC, R.III, Defendants' Cross-Motion, ex. 8, 1. Du Pont actually designed and constructed the plant which it subsequently operated, 179 F.Supp. at 16. Sandia simply stepped in to replace another contractor in a going concern, U.S. Dept. of Energy, *DOE Research & Development & Field Facilities*, June, 1979, IV-112. Du Pont's purchase orders stated that purchases were "for the benefit of the United States Government", 179 F.Supp. at 18. Sandia is required to order in its own

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[16] Since most of its contractors receive fees, the United States is reluctant to read *Livingston's* use tax exemption as hinging on du Pont's no-fee contract. Also, in minimizing *Livingston*, it is hoping to minimize *United States v. Boyd*, which is dispositive of the present case. However, the principles enunciated in *Boyd* transcend the particular tax at issue there.

name and its purchase orders contain no language equivalent to that utilized by du Pont, J.A. 36-37.

Furthermore, unlike du Pont, Sandia and its parent company receive numerous benefits under their contract, making *Livingston* inapplicable. While patents to all discoveries by du Pont belonged to the United States, 179 F.Supp. at 17, Sandia's parent companies receive non-exclusive, irrevocable royalty-free licenses under patents arising from Sandia's work for AEC, J.A. 35. Sandia is affiliated with a parent company that has made over *six billion dollars of profit-making sales* to the United States government between 1966 and 1975, R.IV, Interrog. 44, ex. 2, June 22, 1977.[17] Sandia's profit-making parent is further benefited because the salaries of some of its employees are borne by Sandia, subject to reimbursement under its contract with AEC. For example, these salaries totalled $312,000 in 1975, R.IV, Interrog. 40, Aug. 31, 1976. The parent is also paid by Sandia for audit services and other supervision, again subject to reimbursement from AEC under the contract, J.A. 40-42.

While the district court in *Livingston* minimized du Pont's non-monetary benefits, 179 F.Supp. at 23, there are business advantages for AEC contractors more valuable than any fees:

> The acquisition of invaluable technical and engineering information and experience; the establishment of a reputation as a pioneer in an incalculably great industrial field; the opportunity to gain a march on future competitors (perhaps the opportunity to enjoy an at least temporary monopoly); the possibility of acquiring

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[17] Western Electric is a party to the contract with Sandia and the United States here, R. II, Plaintiff's Motion For Summary Judgment, ex. 3 to Roser Affidavit, 45.

> valuable patents as an outgrowth of research and development activities conducted at federal expense.
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> Newman, *The Atomic Energy Industry: An Experiment in Hybridization*, 60 Yale L.J. 1263, 1320 (1951).

In *Livingston*, the court concluded that du Pont entered its contract "without hope of gain" and out of a "high sense of public responsibility" and acted as the "alter ego" of the Atomic Energy Commission, 179 F.Supp. at 18, 23. This Court's affirmation of these conclusions must certainly have been bolstered by a remarkable stipulation by the State of South Carolina, which is quoted at page 19 of the Motion to Affirm before this Court in that case:

> Each and every operation carried on by du Pont in the procurement and physical use of the material here involved was solely on behalf of the United States. Du Pont did not, as a matter of fact exercise any separate interest in the property involved. Its procurements were solely on behalf of the United States. Its physical use of the property owned by the United States was to accomplish the aims of the United States. At no time did du Pont have the beneficial use of such property for its private ends.

No equivalent stipulation will be found in the present case. The fact that this Court affirmed the three-judge decision solely on a Motion to Affirm, without briefs and oral arguments, weakens the vitality of *Livingston* as a precedent applicable to Sandia. An affirmance without opinion does not carry the precedential weight of an opinion on the merits, *Tully v. Griffin*, 429 U.S. 69 (1976).

Current regulations lay down the circumstances in which some management contractors will receive fees and others will not. What may have been determined by a contractor's "high sense of public responsibility" twenty years ago, *United States*

v. Livingston, 179 F.Supp. 9, 23 (1959), is now routinized by regulation.

Basically "[t]he determination of a fair and reasonable profit or fee is a matter of sound business judgment", J.A. 209. For example, it is ERDA policy "not to pay fees under contracts with educational institutions", J.A. 212. On the other hand, "[i]t is general ERDA policy to pay fees in contracts with not-for-profit organizations; however, *it is a matter of negotiation whether a fee will be paid in a given case*", J.A. 211, emphasis added.

The determination of whether a not-for-profit organization [which Sandia is not] receives a fee is not determined by its degree of patriotism. Instead, "[i]n computing the amount of fee to be paid, take into account *the tax posture* of the not-for-profit organization," J.A. 212, para. (c), emphasis added.

No-fee contracts are not unique to the Atomic Energy Commission. Approximately 2% of all military procurements by the Department of Defense are also on a no-fee basis, Department of Defense, *Military Prime Contract Awards: Fiscal Year 1979*, April 30, 1980, 78. It is unlikely that the Atomic Energy Commission's regulations were intended to identify some contractors as no-fee agents and some as independent contractors purely on the basis of the fees they receive.[18]

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[18] There are "above the line" benefits even when no fee is received. At the time that du Pont operated the South Carolina facility, the General Electric Company operated AEC's Hanford facility for a fee of $1.00 a year. The then-Chairman of the Atomic Energy Commission recorded that General Electric didn't "want to get tarred with the . . . 'merchants of death' . . . brush, don't [sic] want to make profit out of it", Lilienthal, *The Journals of David E. Lilienthal*, Vol. II, Harper & Rowe, New York, 1964, 607. However, General Electric also received a payment for "factory overhead" ranging from 119% to 143% of direct labor costs and "administrative overhead" of $200,000 per month. This prompted a congressional investigation amid complaints that the dollar-a-year fee was deceptive, *Hearings before*

(Cont. p. 39)

The New Mexico tax is, as its name indicates, a tax on a contractor's gross receipts. It is levied regardless of whether the contractor makes a profit, loses money or breaks even, *New Mexico Enterprises, Inc. v. Bureau of Revenue*, 86 N.M. 799, 528 P.2d 212 (Ct.App. 1974). Unless an entity has a 501(c)(3) exemption, which Sandia does not, it must pay tax on its total gross receipts.

V. ABSENT EXPLICIT AUTHORIZATION BY THE UNITED STATES CONGRESS, EXECUTIVE BRANCH PERSONNEL MAY NOT INSULATE PRIVATE CONTRACTORS FROM STATE TAXES BY DESIGNATING THEM AS AGENTS.

In *James v. Dravo Contracting Company*, 302 U.S. 134 (1937), this Court swept away over a century of caselaw stringently limiting the states' power to tax private entities even remotely connected with the federal government,[19] and approved

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[18] (Cont. from p. 38)
the Sub-Committee of the Committee on Appropriations, U.S. Sen., on Independent Offices Bill for 1950, 81st Cong., 1st Sess., 1271 *et seq.*, May 11, 1949. Certainly the *Livingston* court would never have viewed the General Electric Company as a tax free agent, based on its "high sense of public responsibility", 179 F.Supp. 9, 23 (1959). While Sandia's parent company receives certain overhead payments, they do not rival those received by General Electric. Nevertheless, the General Electric experience demonstrates that a contractor's tax immunity should not hinge on a judicial determination of patriotic or charitable motives in not accepting a fee.

[19] Examples are decisions forbidding gross receipts taxes on government contractors, *Panhandle Oil Co. v. Mississippi ex rel. Knox*, 277 U.S. 218 (1928); income taxes on the wages of federal employees, *Dobbins v. Commissioners of Erie County*, 41 U.S. (16 Pet.) 435 (1842); and taxes on the profits derived from exploitation of oil and gas leases on Indian lands, *Gillespie v. Oklahoma*, 257 U.S. 501 (1922).

application of state taxes so long as they were non-discriminatory and so long as their legal incidence did not touch the United States. This Court dealt with high principles in *James v. Dravo,* principles defining the constitutional boundaries of the competitive relationship among federal and state governments in the all-important field of taxation. To those who administer these governments, faced with either the threat of new liabilities or the promise of new revenues, the issue may not have been so much high principles as the prospect of large sums ultimately to be derived from each other's treasuries.

The constitutional distinction between taxes falling directly on the federal government and taxes falling on its contractors exposed the United States to the newly-imposed burden of its contractors' taxes in some states. In such states, officials of the Executive Branch now sought ways to shift the legal incidence to the United States *contractually,* unilaterally conferring immunity on its contractors. The primary strategy has been to assert that a contractor is an agent of the federal government, insulating its purchases and expenditures from state taxes. The agency contention is sometimes based on selectively inserted clauses designating a contractor as an agent; in other cases, the overall relationship is asserted to prove agency in the absence of formal recognition of the status.

This practice, potentially vitiating *James v. Dravo Contracting Company,* was approved in regard to dealings with suppliers in *Kern-Limerick, Inc. v. Scurlock,* 347 U.S. 110 (1954). There, this Court held that statutory authority to negotiate contracts "of any type which . . . will promote the best interests of the Government" authorized the drafting of contracts and purchase orders which designated a private contractor as an agent, thereby insulating the contractor from state taxes, 347 U.S. 114, 116. Noting the similarities of operation between the contractor in *Kern-Limerick* and the contractor held taxable in *Alabama v. King & Boozer,* 314 U.S. 1 (1941), this Court stated that "the

form of contracts, when governmental immunity is not waived by Congress, may determine the effect of state taxation on federal agencies . . .", at 122-123.

The Executive Branch agencies enter into thousands of contracts with private contractors every year. Having interpreted the statutory power to contract as Congressional permission to insulate contractors from state taxes, the *Kern-Limerick* decision has placed the balance of federal-state tax relations completely in the hands of Executive Branch contracting officials, numbering in the thousands.[20] While the Atomic Energy Commission has neglected for policy reasons to avail itself of *Kern-Limerick's* shelter in the present case, *Kern-Limerick* extends the promise that the AEC's relations with its contractors may ultimately be structured to escape state taxes.

Kern-Limerick stands as an anomaly in resolving momentous federal-state issues on the basis of chance contract clauses. As recently as July of 1981, this Court took a far different position in a commerce clause context, approving a lower court observation that, "[i]t would be strange indeed if the legality of a tax could be made to depend on the vagaries of the terms of contracts", *Commonwealth Edison Co. v. Montana*, 49 U.S.L.W. 4957, 4960, n.8 (1981). This echoed Justice Douglas' dissent in *Kern-Limerick:*

> The concepts "title," "agency," and "obligation to pay" are no basis for this constitutional adjudication. Today they are used to permit any government functionary to draw the constitutional line by changing a few words in a contract . . . We should hold that, until the Congress says differently, the States are free to tax all sales to cost-plus government contractors.
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> 347 U.S. at 126-127 (1954) (Douglas, J., dissenting).

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[20] There are 5,000 contracting officers in the Department of Defense alone, Pace, *Negotiation and Management of Defense Contracts*, John Wiley & Sons, 1970, 19.

Indeed, this Court adopted Justice Douglas' formulation, in a slightly different context, in one of the three Michigan "property cases" decided four years later. There, the Court refused to look to the formalities of the contract between the United States and the contractor to determine whether the latter was immune: "Constitutional immunity from state taxation does not rest on such insubstantial formalities as whether the party using government property is formally designated a "lessee". *Otherwise immunity could be conferred by a simple stroke of the draftsman's pen." United States v. Township of Muskegon,* 355 U.S. 484, 486 (1958), emphasis added.[21]

In *Kern-Limerick* this Court held that, once the Executive Branch had unilaterally assimilated a private entity into the government, it was for Congress to "waive" that immunity, 347 U.S. at 122-123. Generally, this Court has taken a different approach: that it is for Congress to *grant* immunity to private entities.[22] In *City of Detroit v. Murray Corporation,* 355 U.S.

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[21] Even in the *Kern-Limerick* decision itself, this Court acknowledged precedents holding that "One acting as a private agent may be bound, notwithstanding his known agency, upon contracts which he executes in his own name", *United States Shipping Board Merchant Fleet Corp. v. Harwood,* 281 U.S. 519, 524 (1929), cited at 347 U.S. 121, n. 10. In that latter case, this Court held that precisely because the contractor was a corporation and because all its money came from the United States, "[t]here is thus no basis for presuming that the Fleet Corporation is not to be deemed bound by the contracts into which it enters merely because it is acting as such an agency. . .", *id.*, at 525.

[22] *Kern-Limerick* is also anomalous in its departure from the doctrine that, "the silence of Congress, when it has authority to speak, may sometimes give rise to an implication as to the Congressional purpose. . . But there is little scope for the application of that doctrine to the tax immunity of governmental instrumentalities," *Graves v. New York,* 306 U.S. 466, 479-480 (1939). Thus, "Silence of Congress implies immunity no more than does the silence of the Constitution," *id.*, 480. Similarly, in refusing to find a Congressional intent to exempt personal property of Indians

(Cont. p. 43)

489 (1958), this Court stated that, ". . . the Congress is the proper agency . . . to make the difficult policy decisions necessarily involved in determining whether and to what extent private parties who do business with the Government should be given immunity from state taxes." Similarly, in holding that two AEC contractors were neither federal agents nor instrumentalities, this Court stated, ". . . it is for Congress, in the valid exercise of its proper powers. . ." to grant state tax immunity if it chose, *United States v. Boyd*, 378 U.S. 39, 51 (1964). Again, in affirming *Livingston v. United States*, 179 F.Supp. 9 (1960), this Court implicitly approved dictum that "It is frequently said that Congress has the power to extend the immunity of the United States beyond the constitutional limits, *but a contracting officer has no such power. . .*", at 20, emphasis added.

Following the *Kern-Limerick* decision, legislation to reverse its impact was promptly introduced.[23] Although none of the bills passed, they achieved their intended purpose when the Department of Defense, the chief beneficiary of the *Kern-Limerick* decision, promised Congress "that it will be the policy of the Department of Defense not to designate prime contractors on cost-type contracts to be performed within the continental limits of the United States, as agents of the Government

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[22] (Cont. from p. 42)
from the Oklahoma estate tax, it was held that, "[t]his Court has repeatedly said that tax exemptions are not granted by implication . . . If Congress intends to prevent the State of Oklahoma from levying a general non-discriminatory estate tax applying alike to all its citizens, *it should say so in plain words.* Such a conclusion cannot rest on dubious inferences." *Oklahoma Tax Commission v. United States*, 319 U.S. 598, 606-607 (1943), emphasis added.

[23] These included H.R. 7206/S.2100, 84th Cong., 1st Sess. (1955); S.6, 85th Cong., 1st Sess. (1957); and H.R. 6057, 87th Cong., 1st Sess. (1961). S.6 was passed by the Senate on March 4, 1958.

for the purchase of supplies", Jan. 28, 1955, Letter from Deputy Assistant Secretary of Defense to Director, Bureau of Budget; J.A. 214; *Hearings Before a Subcomm. of the Comm. on Gov't Operations, 85th Cong., 1st Sess., on S.6,* June 11-12, 1957, 75: These developments suggest that this Court may have misread Congress' intent to empower the Executive Branch to insulate its contractors from state taxes.

There is a disturbing twist to the enactment of this Defense Department policy which illustrates the dangers of relying on the Executive Branch to fairly maintain the balance between state and federal interests. Although it had promised Congress not to insert agency-creating clauses, the Defense Department continued to argue in case after case that its contractors *were* agents, *Boeing Company v. Omdahl,* 169 N.W.2d 696 (N.D. 1969); *State ex rel. Thompson-Stearns-Roger v. Schaffner,* 489 S.W.2d 207 (Mo. 1973); *Day & Zimmerman, Inc. v. Calvert,* 519 S.W.2d 106 (Texas 1974), *cert. denied,* 423 U.S. 832 (1976); *United States v. New Mexico,* 581 F.2d 803 (10th Cir. 1978).[24]

While the Atomic Energy Commission has not been as aggressive as the Department of Defense, the self-conscious attempts by AEC attorneys in drafting the 1977 modifications to come within *Kern-Limerick* while preserving every possible advantage of non-agent status, J.A. 62-80, and the almost comic machinations of the AEC attorney who, in 1968, inserted clauses in

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[24] After the Defense Department's policy and conflicting practice came to light in the cited New Mexico case, the Department "reiterated its 1955 policy statement not to designate cost contractors as agents", agreed that general contract clauses "lend little support for contending that contractors are agents", and agreed that, in future, alternative clauses and practices would be devised to accomplish their "nontax purposes" without providing a basis for an agency contention, Friedman, *The State Tax Liability of Federal Contractors,* Revenue Administration, 1977, Natl. Assn. of Tax Administrators, Wash., D.C., 1977, 65, 72.

the Zia contract expressly denying any agency status in the mistaken belief that it would still be immunized by other clauses, R.IV, Interrog. 11, Feb. 7, 1977; R.V, ex. 17-A, illustrate the inevitable consequences when determinations in this area are left to those most responsible for their budgetary impact.

At least two commentators have criticized the *Kern-Limerick* rationale, see Tribe, *Intergovernmental Immunities in Litigation, Taxation, and Regulation: Separation of Powers Issues in Controversies About Federalism*, 89 Harv. L.R. 682 (1976); Mahoney, *Federal Immunity From State Taxation: A Reassessment*, 45 U.Chi.L.R. 695 (1978). Professor Tribe questions why the United States should ". . . ever be allowed to cut off state revenue sources without congressional action – a power denied the executive when it assumes the economic burden of a tax but neglects the incantation of that magic language," 89 Harv. L.R. at 710.

Because the actions by federal contracting officers in inserting agency-creating clauses occur sporadically and only in those states where taxation is threatened, they are not subject to systematic scrutiny by either the Executive Branch or Congress. Congress alone is in a position to review the varying tax structures of all the states and the federal government.

In *M'Culloch v. Maryland*, 17 U.S. (4 Wheat.) 316 (1819), this Court recognized that its blanket prohibition of state taxation of federal activities might "not extend to a tax paid by the real property of the bank, in common with the other real property within the State, nor to a tax imposed on the interest which the citizens of Maryland may hold in this institution, in common with other property of the same description throughout the State", *id.*, at 436. While the Marshall court repudiated its own dictum in *Weston v. City Council*, 27 U.S. (2 Pet.) 449, 468-469 (1829), against a strong dissent, *id.*, at 472-473 (Johnson, J.,

dissenting), the theme that only discriminatory state taxation of federal operations is prohibited under the constitution has endured. In *United States v. County of Fresno*, 429 U.S. 452 (1977), this Court read the above quote from *M'Culloch* with a non-discrimination gloss, 429 U.S. at 459, noting that

> [f]or many years the Court read the decision in M'Culloch as forbidding taxes on those who had contractual relationships with the Federal Government . . . In later years, however, the Court departed from this interpretation of M'Culloch,
>
> *Id.*, at 460.

Thus, this Court has come close to adopting the observation that

> One could, and perhaps should, read M'Culloch . . . simply for the principle that the Constitution prohibits a state from taxing discriminatorily a federally established instrumentality,
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> *First Agricultural National Bank v. State Tax Commission*, 392 U.S. 339, 350 (1968) (Marshall, J., dissenting).

The case for approving non-discriminatory taxation of private entities related to the United States only through contracts is far stronger. New Mexico urges that this Court reconsider its holding in *Kern-Limerick*, as either a misreading of Congressional intent or as an unwarranted restriction on the power of the states to levy non-discriminatory taxes whose legal incidence falls on private contractors, not on the United States.

CONCLUSION

The judgment of the court of appeals should be affirmed.

Respectfully submitted,

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APPENDIX A – N.M. Stat. Ann. 1953

§72-16A-2. **Purpose.**–The purpose of the Gross Receipts and Compensating Tax Act is to provide revenue for public purposes by levying a tax on the privilege of engaging in certain activities within New Mexico and to protect New Mexico businessmen from the unfair competition that would otherwise result from the importation into the state of property without payment of a similar tax.

§72-16A-3(K). [(as amended) (Supp. 1978)] "service" means all activities engaged in for other persons for a consideration, which activities involve predominantly the performance of a service as distinguished from selling property. In determining what is a service, the intended use, principal objective or ultimate objective of the contracting parties shall not be controlling.

* * *

§72-16A-12.17. **Exemption; gross receipts tax; certain organizations.**–Exempted from the gross receipts tax are the receipts of organizations that demonstrate to the bureau that they have been granted exemption from the federal income tax by the United States commissioner of internal revenue as organizations described in Section 501(c)(3) of the United States Internal Revenue Code of 1954, as amended or renumbered. This section does not apply to receipts derived from an unrelated trade or business as defined in Section 513 of the United States Internal Revenue Code of 1954, as amended or renumbered.

§72-16A-14.9. [(as amended) (Supp. 1978)] **Deduction; gross receipts tax; sales to governmental agencies.**–Receipts from selling tangible personal property, other than nonfissionable metalliferous mineral ore, to the United States or any agency or instrumentality thereof or the state of New Mexico or any political subdivision thereof may be deducted from gross receipts. Receipts from selling tangible personal property, other

than nonfissionable metalliferous mineral ore, to the governing body of an Indian tribe or Indian pueblo for use on Indian reservations or pueblo grants may be deducted from gross receipts. That portion of the receipts from performing a service as defined in Subsection K of Section 7-9-3 [§72-16A-3] NMSA 1978 which reflects the value of tangible personal property utilized or produced in performance of such service is not deductible.

APPENDIX B – 41 U.S.C. §255

Advance or other payments; restrictions; conditions

(a) Any executive agency may–

(1) make advance, partial, progress or other payments under contracts for property or services made by the agency; and

(2) insert in bid solicitations for procurement of property or services a provision limiting to small business concerns advance or progress payments.

(b) Payments made under subsection (a) of this section may not exceed the unpaid contract price.

(c) Advance payments under subsection (a) of this section may be made only upon adequate security and a determination by the agency head that to do so would be in the public interest. Such security may be in the form of a lien in favor of the Government on the property contracted for, on the balance in an account in which such payments are deposited, and on such of the property acquired for performance of the contract as the parties may agree. This lien shall be paramount to all other liens.

APPENDIX C – Section 4(c)(2) of the Atomic Energy Act of 1946, 60 Stat. 759, now codified at 42 U.S.C. § 2061(b)

OPERATION OF THE COMMISSION'S PRODUCTION FACILITIES.– The Commission is authorized and directed to produce or to provide for the production of fissionable material in its own facilities. To the extent deemed necessary, the Commission is authorized to make, or to continue in effect, contracts with persons obligating them to produce fissionable material in facilities owned by the Commission. The Commission is also authorized to enter into research and development contracts authorizing the contractor to produce fissionable material in facilities owned by the Commission to the extent that the production of such fissionable material may be incident to the conduct of research and development activities under such contracts. Any contract entered into under this section shall contain provisions (A) prohibiting the contractor with the Commission from subcontracting any part of the work he is obligated to perform under the contract, except as authorized by the Commission, and (B) obligating the contractor to make such reports to the Commission as it may deem appropriate with respect to his activities under the contract, to submit to frequent inspection by employees of the Commission of all such activities, and to comply with all safety and security regulations which may be prescribed by the Commission. Any contract made under the provisions of this paragraph may be made without regard to the provisions of section 3709 of the Revised Statutes (U.S.C., title 41, sec. 5) upon certification by the Commission that such action is necessary in the interest of the common defense and security, or upon a showing that advertising is not reasonably practicable, and partial and advance payments may be made under such contracts. The President shall determine at least once each year the quantities of fissionable material to be produced under this paragraph.

APPENDIX D – 31 C.F.R. Part 205 (1976)

PART 205–WITHDRAWAL OF CASH FROM THE TREASURY FOR ADVANCES UNDER FEDERAL GRANT AND OTHER PROGRAMS

Sec.

205.1 Purpose.
205.2 Scope of regulations.
205.3 General policy.
205.4 Treasury check.
205.5 Letter of credit.
205.6 Secondary recipients.
205.7 Termination of advance methods of financing grant programs.
205.8 Single letter of credit.
205.9 Responsibility of program agencies.
205.10 Implementing instructions.
205.11 Waivers.

AUTHORITY: 5 U.S.C. 301 and sec. 203, 82 Stat. 1101, 42 U.S.C. 4213.

SOURCE: The provisions of this part contained in Department Circular 1075, 3d Revision, 38 F.R. 5242, Feb. 27, 1973, unless otherwise noted.

§ 205.1 Purpose.

Federal grant and other programs involving advances to various organizations outside the Federal Government constitute a significant portion of the Federal budget. Advances of cash from the Treasury to such organizations (thereinafter called recipient organizations) for the purpose of financing their current operations under the Federal programs have a substantial impact on Treasury financing costs and the level of the public debt. The purpose of this part is to prescribe the timing of such advances and the procedures to be observed to assure that cash withdrawals from the Treasury occur only when

essential to meet the needs of a recipient organization for its actual disbursements.

§ 205.2 Scope of regulations.

(a) The regulations in this part cover disbursement practices for all cash advances to recipient organizations (including States and local governments, educational institutions, international organizations, and any other public and private organizations) under Federal grant or other programs. The regulations also establish guidelines to be observed by Federal program agencies with respect to their responsibilities in executing grant and other programs, including their review of recipient organization practices in obtaining cash advances by drawing on letters of credit and otherwise. Coverage applies to any Federal program requiring advances to finance the recipient organization's activities in carrying out the program, whether by contract, grant, contribution, or other form of agreement. (Advance payments on procurement contracts are also subject to the provisions of the Federal Procurement Regulations regarding contract financing which appear at 41 CFR Part 1-30 and the provisions of the Armed Services Procurement Regulations regarding defense contracting which appear at 32 CFR Part 163.) Although the regulations of this part are not generally applicable to loan programs, the letter-of-credit method described in § 205.5 should be considered by program agencies for application to loans carrying interest rates which are lower than Treasury borrowing rates.

(b) These regulations are not intended to apply to Government disbursements made to reimburse an organization for work already performed and financed with the organization's own working capital. However, these regulations do apply to reimbursable grant programs involving nonprofit organizations participating in the single letter-of-credit funding system as outlined in § 205.8. Any other specific application of features of these

regulations to reimbursement payments will be considered by the Department of the Treasury if requested by a program agency.

§ 205.3 General policy.

Regardless of the particular method used, advances to a recipient organization shall be limited to the minimum amounts needed and shall be timed to be in accord only with the actual, immediate cash requirements of the recipient organization in carrying out the purpose of the approved program or project. The timing and amount of cash advances shall be as close as is administratively feasible to the actual disbursements by the recipient organization for direct program costs and the proportionate share of any allowable indirect costs.

§ 205.4 Treasury check.

When the annual advance to a recipient organization is less than $250,000 or if the annual advance to a recipient organization aggregates more than $250,000 but there is not a continuing relationship for at least 1 year, the advance shall ordinarily be made by Treasury check. Advances by Treasury check shall be made only in amounts necessary to meet current disbursement needs. Program agencies shall schedule advances made by Treasury check so that the funds are available to the recipient organization only immediately prior to their disbursement by the organization. Therefore, if disbursements are made by the recipient organization on a monthly, biweekly, or any other regular cycle, and the amounts involved would so warrant, the issuance of Treasury checks shall be similarly timed.

§ 205.5 Letter of credit.

(a) If a program agency has, or expects to have a continuing relationship with a recipient organization for at least 1 year, involving annual advances aggregating at least $250,000, the agency shall use the letter-of-credit method.

(b) This method provides program agencies, recipient organizations, and the Department of the Treasury with mechanics specifically designed to enable a recipient organization to obtain cash from Treasury promptly and with such frequency as may be necessary based upon its own determination of when and how much is actually needed for its disbursements.

(c) A letter of credit, which must be executed by an authorized certifying officer of the program agency concerned, gives the recipient organization the authority to draw directly on the Treasury, through its commercial bank (acting as its agent) and either a Federal Reserve Bank (acting as agent of the Treasury) or the Division of Cash Services, Bureau of Government Financial Operations, subject to any monetary and other limits established by the program agency. Withdrawals must be made by authorized officials of the recipient organization designated by it and approved by the program agency's certifying officer.

(d) A letter of credit is irrevocable (the equivalent of cash available to the recipient organization) to the extent the recipient organization has obligated funds in good faith thereunder in executing the authorized Federal program in accordance with the grant, contract, or other agreement.

(e) Use of letters of credit shall be covered by a clause in the grant, contract, or other financing agreement whereby the recipient organization commits itself to (1) the practice of initiating cash drawdowns only when actually needed for its disbursements, (2) the timely reporting of cash disbursements and balances as required by the program agency, and (3) the imposition of the same standards of timing and amount upon any secondary recipients including the furnishing of reports of cash disbursements and balances, with the understanding that failure to adhere to these provisions may cause the unobligated portion of the letter of credit to be revoked by the program agency or by the Department of the Treasury. The financial management system of the recipient organization shall provide

for effective control over and accountability for all Federal funds. With respect to State and local governments, this is stated in OMB Circular A-102.

(f) Drawdowns shall not ordinarily be made more frequently than daily, or be in amounts less than $10,000 or more than $1 million, but in no case more than $5 million unless so stated on the letter of credit.

(g) Since the letter-of-credit method enables the recipient organization to withdraw cash from the Treasury concurrently with and as frequently as disbursements are made by the recipient, there need be no time lag between drawdowns from the Treasury and disbursements by the recipient organization. Therefore, there is no necessity for the recipient organization to maintain balances of Federal cash other than the small balances necessary to accommodate the minimum limitation on individual drawdowns as provided for in paragraph (f) of this section and to provide for an element of bank float.

(h) In general, agreements shall provide for a recipient organization to initiate each drawdown at approximately the same time that checks are issued by the organization in payment of program liabilities, including those for allowable indirect costs, and in an amount approximately equal to the Federal share of such payments. In order to take advantage of the float on checks outstanding, program agencies wherever possible should arrange for recipient organizations to delay drawdowns on letters of credit until after the checks issued for program disbursements have been forwarded to the payees.

(i) In specific instances, as determined mutually by the Department of the Treasury and the program agency, a recipient organization may be requested to authorize its commercial bank to draw on a letter of credit in its behalf when checks issued by the recipient organization (covering disbursements of Federal funds) are presented to the bank for payment.

§ 205.6 Secondary recipients.

(a) Advances made by primary recipient organizations (those which receive payments directly from the Federal Government) to secondary recipients shall conform substantially to the same standards of timing and amount as apply to advances by Federal agencies to primary recipient organizations.

(b) Federal program agencies should encourage primary recipient organizations to develop procedures, similar to the Federal letter of credit, whereby secondary recipients can draw on the primary recipient as funds are needed for disbursement, in lieu of the primary organization advancing funds to the secondary recipient organization.

§ 205.7 Termination of advance methods of financing grant programs.

(a) When a recipient organization receiving advances by a letter of credit or by Treasury check has demonstrated to a program agency an unwillingness or inability to establish procedures that will minimize the time elapsing between advances and the disbursement thereof, the program agency, if permitted by the statutes governing the grant(s) in question, shall require the recipient organization to finance its operations with its own working capital, and payments to the recipient organization shall be made by Treasury check to reimburse it for actual cash disbursements. Program agencies shall process such reimbursements expeditiously so as to minimize the time elapsing between disbursement by and payment to the recipient organization.

(b) In those cases when the reimbursement method described in paragraph (a) of this section is not feasible, arrangements may be made whereby the operations of the recipient organization are financed on a working capital advance basis. On this basis, funds may be advanced to the recipient organization to cover its estimated disbursement needs for a given initial period. Thereafter, the recipient organization would be reimbursed for

the amount of its actual cash disbursements. The amount of the initial advance shall be geared to the reimbursement cycle so that after the initial period the advance approximately equals the average amount of the recipient organization's unreimbursed program payments.

§ 205.8 Single letter of credit.

(a) The single letter of credit is basically the replacement of numerous letters of credit held by a recipient organization with one letter of credit administered centrally. It provides the mechanics for a single flow of funds between the Federal Government and the particular recipient organization.

(b) Each Federal program agency should work toward the objective of establishing a single letter of credit with each State government. As a first step, each program agency should consolidate its own internal procedures to provide for a single letter of credit being issued to each State to fund all the programs of that Federal agency as a whole. In addition, each program agency should join with the Department of the Treasury in efforts to achieve a single letter of credit from the Federal Government as a whole to each of the States.

(c) When a single letter of credit is established with a State, Federal program agencies may include in the single letter of credit, subject to the provisions of paragraph (d) of this section, reimbursable grant programs and also smaller grant programs which do not meet the $250,000 yearly limitation otherwise required in the use of letters of credit.

(d) The implementation of a single letter of credit with a State shall first be approved by Treasury and must be covered by a written agreement whereby the State obligates itself to the provisions outlined in § 205.5(e). The agreement must also indicate that the Department of the Treasury reserves the right to revoke the letter of credit in the event of noncompliance with any of these provisions.

(e) If requested by a program agency, the Department of the Treasury will consider application of the single letter of credit to include recipient organizations other than State governments.

(f) The single letter of credit is a significant step in the simplification of Federal grant-in-aid funding and provides for a more effective means of administering the letter-of-credit method of funding grant-in-aid programs. The single letter of credit, as designed, will minimize the cash flow from Treasury with substantial savings and will facilitate sound cash management principles on the part of the recipient organizations.

§ 205.9 Responsibility of program agencies.

Regardless of the particular method used to advance funds, the program agency is responsible for (a) making such reviews of the financial practices of recipient organizations, both primary and secondary, as are necessary to insure that the provisions of this Part 205 are being complied with, and (b) instituting such remedial measures as may be necessary in the event that a recipient organization demonstrates its unwillingness or inability to comply with these provisions. Implementing procedures of program agencies shall specify the methods employed to carry out these responsibilities. Also, each program agency shall furnish the Department of the Treasury with reports, semiannually, showing cash balances in the hands of the recipient organizations as of each June 30 and December 31.

§ 205.10 Implementing instructions.

Implementing procedural requirements under this part will be promulgated by the Commissioner of the Bureau of Government Financial Operations in the Treasury Fiscal Requirements Manual for Guidance of Departments and Agencies.

§ 205.11 Waivers.

Any waivers of provisions of this part previously granted to program agencies are hereby revoked. Requests for waivers of

specific provisions of this part shall be presented in writing to the Commissioner of the Bureau of Government Financial Operations.

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No. 80-702

In the Supreme Court of the United States

OCTOBER TERM, 1981

UNITED STATES OF AMERICA, PETITIONER

v.

STATE OF NEW MEXICO, ET AL.

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE TENTH CIRCUIT

REPLY BRIEF FOR THE UNITED STATES

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REPLY BRIEF FOR THE UNITED STATES

1. In seeking affirmance of the decision below, New Mexico takes issue with our submission that Sandia, Zia, and LACI were procurement agents of the United States. It urges (Br. 5-7) that these contractors were not agents under the standard Department of Energy contract for the management of a government-owned atomic facility because the purchases were made in the name of the contractors, rather than in the name of the United States. Moreover, New Mexico asserts (Br. 26-27) that the advanced funding procedure has no relevance because it does not accord a supplier a claim against the United States, but simply provides a mechanism to insure prompt payment of obligations incurred by the private contractors under the contract and to guarantee that the government will be able to retrieve any undisbursed funds.

But it can scarcely be doubted that the United States can purchase supplies or services through private persons without relinquishing its constitutional immunity from state

taxation. The Court's decision in *Kern-Limerick, Inc.* v. *Scurlock*, 347 U.S. 110 (1954), upon which we rely, firmly establishes that proposition. There, as here, a consortium of private companies purchased equipment on behalf of the government for use in performing a government contract. In holding the transactions immune from the Arkansas sales tax, the Court "[found] nothing in the Procurement Act that bars a contract for purchase for the United States of supplies or services by private persons" and "that the Navy Department has power to negotiate contracts which provide for private purchasing agents for supplies and materials" (*id.* at 116).

To be sure, in *Kern-Limerick* the contract provided that "[t]he Contractor shall act as the purchasing agent of the Government in effecting such procurement and the Government shall be directly liable to the vendors for the purchase price" (347 U.S. at 112 n.2). But the fact that the private contractors were the nominal "Buyers" under the standard DOE contract at issue here does not distinguish this case from *Kern-Limerick*. In conformity with the arrangement spelled out in the bid and purchase orders in *Kern-Limerick*, here, as well, "[t]he Government [was] obligated to the Vendor for the purchase price, but the Contractor shall handle all payments * * * on behalf of the Government" (*id.* at 119).

As we have discussed in greater detail in our opening brief (at 32-35), the government's obligation to the vendors to pay the purchase price is a direct consequence of the advance funding procedure. That procedure, as New Mexico points out (Br. 7-8, 26), may serve other purposes such as acheiving prompt payment.[1] But its significance for

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[1]New Mexico also points out (Br. 28) that there are more than 10,000 recipients of government funds that are parties to comparable advance funding arrangements but that they are not agents of the government. We agree. Most of these recipients are grantees of government funds

purposes of constitutional tax immunity lies in the fact that every time Sandia, Zia, or LACI issued a check to a third-party supplier or to one of their employees,[2] they were disbursing funds belonging to the United States and thereby automatically obligating the United States at the very outset. Surely the power to spend government money "gave to the contractors the status of agents of the Government to enter into contracts or to pledge its credit." *Alabama* v. *King & Boozer*, 314 U.S. 1, 13 (1941). Indeed, the only credit or cash at risk in the performance of these standard DOE management contracts was the credit and cash of the United States, for the contracts provided that "[n]either Western [Electric] nor Sandia Corporation shall be required to provide funds for operations under this Contract" (J.A. 32). Thus, the practical import of this provision, as implemented by the advance funding procedure, establishes that the obligations under the contracts were those of the government and not of the contractors. If the contractor receiving after-the-fact reimbursement in *Kern-Limerick* was deemed to be an agent of the United States so that sales to it were immune from state taxes, the case for immunity here follows a fortiori because the contractors have the additional authority to disburse government funds in the

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who use them for purposes unrelated to government contracts. Accordingly, this fact does not undermine the significance of advance funding in the instant case, where the contractors are disbursing funds on behalf of the government for goods and services over which the government asserts immediate title and control.

[2]New Mexico (Br. 5-6) emphasizes that 58% of the contractors' disbursements went to meet their own payrolls. But the contractors' employees are on the same footing as the third-party suppliers of goods. The employees simply supply services for a fee. Hence, the contractors' disbursements to suppliers of both goods and services are immune from tax.

first instance, thereby pledging the credit of the United States. See *United States* v. *Forst*, 569 F. 2d 811 (4th Cir. 1978).[3]

2. Both New Mexico (Br. 10) and the amicus Multistate Tax Commission (Br. 12-14) rely upon *United States* v. *Boyd*, 378 U.S. 39 (1964), and claim that the Court there held that contractors under DOE standard management contracts were not agents of the government. As we explained in greater detail in our opening brief (at 23-25, 39-40), the aspect of *Boyd* upon which we rely is the sales tax portion of the case that was considered by the Tennessee Supreme Court, but not appealed to this Court (see 378 U.S. at 43 n.5). Moreover, the use tax involved in the appeal to this Court in *Boyd* was not a compensating use tax of the type involved here but rather a "privilege"-type use tax. The decision of this Court in *Boyd* therefore has no bearing on this case.

The applicable precedent, we submit, is *Kern-Limerick, Inc.* v. *Scurlock, supra*, which establishes the ground rules for tax immunity in connection with the performance of government contracts. Contrary to the assertion of the Multistate Tax Commission (Br. 7), that decision does not "place form over substance and extend implied intergovernmental tax immunity beyond its legitimate scope."

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[3]New Mexico points out (Br. 25) that the contractors' fixed management fees are likewise drawn down under the advanced funding procedure but are concededly subject to its gross receipts tax (see our opening brief at 6 n.3). In its view, this concession undermines the significance of the advance funding procedure with respect to the contractors' other disbursements. The management fee is a payment to the contractors and represents their profits; accordingly, such payments are properly regarded as "gross receipts" under N.M. Stat. Ann. 1953 § 72-16A-3.F (Supp. 1975). With respect to the other disbursements, however, the contractor is merely acting for the government as a paymaster of government funds to third parties. Such funds, therefore, are not taxable as part of the "gross receipts" of the contractor. Compare *United States* v. *County of Fresno*, 429 U.S. 452, 465-466 nn.14, 15. (1977).

Nor does it "stand[] as an anomaly in resolving momentous federal-state issues on the basis of chance contract clauses," as New Mexico contends (Br. 41). If Congress chooses to do so, it may waive the immunity of the United States from state and local taxes. Here, Congress has not chosen to do so. If, as we submit, Zia, Sandia, and LACI are purchasing agents of the government, their purchases are accordingly immune from the New Mexico gross receipts tax. And the relationship between the contractors and the government necessarily turns on the provisions and practical import of the contracts and their mode of implementation. It therefore cannot be seriously questioned that "the form of contracts, when governmental immunity is not waived by Congress, may determine the effect of state taxation on federal agencies, for decisions consistently prohibit taxes levied on the property or purchases of the Government itself" (*Kern-Limerick, Inc.* v. *Scurlock, supra*, 347 U.S. at 122-123; footnotes omitted).

CONCLUSION

For the reasons stated above and in our opening brief, the judgment of the court of appeals should be reversed.

Respectfully submitted.

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Solicitor General

DECEMBER 1981

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ALEXANDER L. STEVAS,
UNITED STATES

No. 80-702

IN THE SUPREME COURT OF THE UNITED STATES

October Term, 1980

UNITED STATES OF AMERICA,

Petitioner,

v.

STATE OF NEW MEXICO, et al.,

Respondent.

ON WRIT OF CERTIORARI TO THE
UNITED STATES COURT OF APPEALS
FOR THE TENTH CIRCUIT

BRIEF ON BEHALF OF STATE OF CALIFORNIA AS AMICUS CURIAE FOR THE STATE OF NEW MEXICO

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No. _____

IN THE SUPREME COURT OF THE UNITED STATES

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INTEREST OF THE AMICUS CURIAE

California has been faced with suits brought by the United States Attorney General claiming tax immunity as "agents" of the United States for various private contractors doing business with the Department of Defense and

other federal agencies arising solely from "magic words" in departmental regulations or other acts which appear to have no function or purpose other than to obtain immunity from state taxation. California believes this is contrary to the intention of this Court as well as that of Congress and the stated policy of Department of Defense. California requests that the Supreme Court by its opinion in this case clearly restrict tax immunity of independent contractors doing business with the United States to those rare circumstances where the need is clear for use by the United States of an independent contractor as its agent for purposes other than tax immunity and the true substance of the transaction as that in which the United States takes full and open responsibility as principal.

California joins in and will not here duplicate the Briefs of New Mexico and the other Amicus Curiae supporting it.

ARGUMENT

THE ATTORNEY GENERAL OF THE UNITED STATES IS ATTEMPTING TO EXPAND TAX IMMUNITY OF GOVERNMENT CONTRACTORS BEYOND THAT INTENDED BY THE JUDICIAL, LEGISLATIVE AND EXECUTIVE BRANCHES OF GOVERNMENT THROUGH USE OF THE "AGENCY" DEVICE

California submits that the King & Boozer, Kern-Limerick, Inc., Livingston and Boyd decisions of this Court show that federal tax immunity should not lightly be extended to government contractors as "agents" of the United States. (See discussion under heading V in New Mexico brief.) This Court should rule that federal immunity is not extended to dealings by independent

contractors except where the United States clearly acts as a true disclosed principal which assumes all the normal duties and responsibilities of a true principal for purposes other than creating tax exemption and the private contractor is clearly acting as an agent for disclosed principal (USA).

"Magic words" merely stating that the contractor acts as agent not accompanied by the clear substantive assumption by the United States of the responsibilities of a principal do not an "agency" make.

Congress clearly has intended to preclude federal employees from immunizing private contractors from state taxes by use of magic words of agency.

In 1939 Congress authorized the Navy to enter into cost plus fixed fee contracts (53 Stats. 590, § 4(a)).

House Bill No. 8438, 76th Congress, Third Session as it came from the Senate to the House of Representatives provided that:

> " . . . all contractors who enter into contracts under the authority contained in this paragraph shall, in the discretion of the Secretary of the Navy, be held to be agents of the United States for the purposes of such contracts and all purchases under such contracts shall be exempt from Federal, State and local taxes."
>
> (86 Cong. Rec. 11401.)

There followed a proposed amendment, debate and elimination of the above quoted "exemption through agency" language. (86 Cong. Rec. 11401-04 [H.R.], 11675 [Senate].)

Continued Congressional intent to prevent private contractors from enjoying a tax immunity is shown by its repeal of 9(b) of the Atomic Energy Act effective October 1, 1953, following

judicial reliance thereon in 1952 (Carson v. Roane-Anderson Co. (1952) 342 U.S. 232) as a basis for immunizing an Atomic Energy Commission contractor from state taxes. (See discussion at page 19 of United States v. Livingston (E.D. S.C. 1959) 179 F.Supp. 9, affd. per curiam 364 U.S. 281.)

About 1954 attempts to immunize corporations doing business with the Navy as "agents" of the United states again came to the attention of Congress. On January 28, 1955[1/] an Assistant Secretary of Defense wrote to a member of Congress, Rowland Hughes,"

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1. This letter is in evidence in United States of America v. State Board of Equalization (U.S.D.C Central Dist. Cal.) Civ. No. 79-02652-R as an attachment to a "Supplemental Declaration. . .," filed March 4, 1980, therein (and appearing at page 191 of "Excerpts of Record" on the appeal therein to the 9th Circuit Court of Appeals No. 80-5391.

"In response to an informal request from your office, we wrote you on May 18, 1954 concerning the designation of contractors as agents of the Government for the purpose of making purchases for Government use. Senator Gore had written Mr. Dodge on March 1, 1954 inquiring as to the extent such procedures; as exemplified in Kern-Limerick-Inc. v. Scurlock (347 U. S. 110, 1954), constituted general policy.

"Our letter advised that the only instances in which a contractor had been constituted as an agent for the Government for the purpose of making purchases and to pledge the credit of the Government therefor, were limited to some cost-plus-a-fixed-fee construction contracts of the Navy. Report was also made of the fact that neither the Army nor the Air Force used the device and that the Navy made no use of it in any other type of contract, including firm fixed-price construction contracts.

"We also indicated that whether use of the purchase-agent device would be extended or continued was being studied by a committee composed of representatives of the military departments as well as the

> Office of the Secretary of Defense. In accordance with our commitment to provide you with the results of that study, we wish to advise that this study has now been completed. It has been determined that it will be the policy of the Department of Defense not to designate prime contractors on cost-type contracts to be performed within the continental limits of the United States, as agents of the Government for the purchase of supplies."

Hearings were thereafter held wherein this policy was reiterated. (See Hearings Before A Subcommittee of The Com. on Gov. Operations United States Senate, 85th Cong., 1st Sess. on S. 6, held June 11 and 12, 1957, pp. 75-78 wherein counsel for the Air Force accompanied by counsel for Department of Defense stated:

> "The Department of Defense has established a firm policy against designating contractors on contracts to be performed within the United States as agents of the Government for the purchase of

> supplies and with the right to pledge the credit of the Government in order to avoid the imposition of taxes."

In apparent reliance on "self-policing" of this nature Congress refrained from passing legislation.

As further evidence of Congress' desire to narrow (rather than broaden) tax immunity of private corporations performing functions for the United States Government, it amended 12 U.S.C. 548 in 1969 (Pub.L. 91-156) to initiate elimination of immunity of national banks from non-discriminatory state taxation.

Action has been taken at the top levels of the Executive branch to narrow claims of tax immunity through "agency." General Services Administration (hereinafter sometimes "GSA") amended its supply schedule

contract regulations about 1969 to eliminate "agency" type language.[2/] The Department of Defense, which established its non-agency policy in 1955 (discussed above), similarly amended its Armed Services Procurement Regulations (ASPR) in 1977 (32 C.F.R. § 5.900 to 5.907).

The need for this Court to clearly and narrowly define the situations in which private contractors as "agents" of the United States can avoid paying state taxes is emphasized by the aggressive efforts in litigation of attorneys for the United States in attempting to extend tax immunity of

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2. "You are hereby authorized to act for the Government. . ." and "This order is placed in behalf of [insert name of department]" were replaced by "This order is placed pursuant to written authorization from [naming government department]" (41 C.F.R. § 1-5.900 to 1-5.905.)

private contractors contrary to the above-described intention to narrow such immunity.

In the early 1970's, without revealing the Department of Defense policy against agency or the 1969 GSA supply schedule regulation amendment, attorneys for the United States of America sought in court immunity from state taxation regarding pre-1973 leases by Department of Defense contractors and pursuant to GSA supply schedules, among others. (U.S.A. v. S.B.E. U.S.D.C., Central Dist. Cal. 72-2568-R.) Thereafter, California became aware of the Department of Defense policy. In United States of America v. State Board of Equalization (dealing with years 1973-76) now pending before the 9th Circuit No. 80-5391, the United States asserts that in spite of the clear

Department of Defense policy not to make its contractors agents, the wording in its ASPR regulation (quoted in footnote 2 above) "in behalf of" and "for" (which were not deleted until 1977) created a tax immune "agency."

In a later federal case (dealing with 1979-present) United States of America v. California State Board of Equalization Civ. No. 79-03359-R (Central District, California) attorneys for the United States are asking the court to declare as a general rule of law that

> "leases of tangible personal property made pursuant to General Services Administration (GSA) supply schedule contracts by contractors having cost-reimbursable contracts with the United States and having been authorized by the United States to use GSA supply schedule contracts were leases made by the contractor as agent of the United States for procurement purposes and, as such, were leases to the United States and

> were not subject to the California sales tax.",

even though the applicable GSA regulations (41 C.F.R. § 1-5.900 to 1-5.905) were amended in 1969 to remove the only language which suggested agency was created when government contractors are authorized to use GSA contracts.

It thus appears that while Congress, the regulations and policies of executive departments, and the rulings of this Court mandate that extension of constitutional immunity to private contractors as agents of the United States be narrowly limited, attorneys for the United States in litigation are attempting to expand such immunity to and beyond the point where mere "magic words" like "in behalf of" or "as agent for" will create immunity even though there is not in substance a true principal-agency

relationship created for legitimate purposes except to establish tax immunity.

Here magic words of "agency" were apparently inserted into contracts by employees in New Mexico two years after this litigation began, with no apparent purpose except to create tax immunity. (See discussion in New Mexico Brief, heading III). Such actions should be held to be ineffective in avoiding taxes.

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CONCLUSION

The opinion of this Court should make it clear that government contractors cannot be immunized from state taxes by a federal department merely stating in a contract that the contractor is authorized to act "in behalf of" or "for" a government department or merely to use GSA supply schedule contracts. The Court should make it clear that only where the United States clearly has complete control of and responsibility for actions of the alleged "agent" and the actions of the alleged agent are clearly those of the United States as principal, can the acts of the alleged agent be immune from state taxation as acts of the United States. The tax immunity of the United states should not apply to acts of any private company

which acts in its own name or otherwise acts independently.

Here, notwithstanding the "magic words" and "advance funding" the alleged agents were not true agents. They had no authority to bind the United States. They are not immune from tax.

Even should the Court find sufficient evidence here that the United States was fully bound as principal under the transactions in issue, that the agents performed no independent acts which were taxable and therefore no tax is payable, the Court should in its opinion make it clear that immunity cannot be created by "magic words" of agency and

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only where in substance the United States is fully bound as the true principal can state taxes be avoided.

Respectfully submitted,

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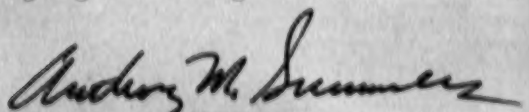

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No. 80-702

UNITED STATES OF AMERICA,

Petitioner,

v.

STATE OF NEW MEXICO, ET AL.,

Respondents.

I, the undersigned say: I am a citizen of the United States, over 18 years of age, employed in the County of San Diego, in which county the within-mentioned mailing occurred, and not a party to the subject cause; my business address is 110 West A Street, Suite 700, San Diego, California 92101.

I served a copy of the BRIEF ON BEHALF OF STATE OF CALIFORNIA AS AMICUS CURIAE FOR THE STATE OF NEW MEXICO on each of the following, by placing same in envelopes addressed as follows:

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Each envelope was then sealed and with the postage prepaid deposited in the United States mail by me at San Diego, California, on July 10, 1981.

There is a delivery service by United States mail at each place so addressed or regular communication by United States mail between the place of mailing and each place so addressed.

I declare under penalty of perjury that the foregoing is true and correct, and this declaration was executed on July 10, 1981, at San Diego, California.

Carolyn C. Yada
CAROLYN C. YADA

Subscribed and sworn to
before me this 10TH day of
July, 1981.

Sandra Zweig
Notary Public in and for said
County and State

OFFICIAL SEAL
SANDRA ZWEIG
NOTARY PUBLIC - CALIFORNIA
PRINCIPAL OFFICE IN
SAN DIEGO COUNTY
My Commission Expires February 26, 1983

Office-Supreme Court, U.S.
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CLERK

NO. 80-702

In The

Supreme Court of the United States

October Term, 1980

UNITED STATES OF AMERICA,

Appellant,

vs.

STATE OF NEW MEXICO, et al.,

Appellees.

On Writ of Certiorari to the United States Court of Appeals for the Tenth Circuit

BRIEF OF AMICUS CURIAE MULTISTATE TAX COMMISSION IN SUPPORT OF APPELLEES

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COUNTERSTATEMENT OF QUESTION PRESENTED

We believe that the question presented is properly stated as follows: Did the lower court properly conclude, under the facts and circumstances of this case, that the legal incidences of the New Mexico gross receipts taxes in question were imposed on the contractors in question as private contractors rather than as agencies of instrumentalities of the United States; and that therefore, under controlling precedent, these contractors were not exempt from the taxes in question under the doctrine of implied governmental immunity?

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Boyd and the cases cited therein control disposition of this case wherein it was held that implied inter-governmental tax immunity is limited to taxes, the legal incidences of which are imposed on agencies or instrumentalities of the United States Government. 11

There is no valid reason why the Judicial Doctrine of Implied Governmental Tax Immunity should be extended to embrance the activities of private corporations which conduct proprietary activities on behalf of governmental agencies unless such private corporations are agencies and instrumentalities of the United States Government. 14

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On Writ of Certiorari to the United States Court of Appeals for the Tenth Circuit

BRIEF OF AMICUS CURIAE MULTISTATE TAX COMMISSION IN SUPPORT OF APPELLEES

INTRODUCTORY STATEMENT

This brief is submitted by the Multistate Tax Commission in support of the Appellees' position. Both parties to this proceeding have consented to the filing of this brief.[1]

[1]Originals of the consent letters have been filed with the Clerk of the Court.

STATEMENT OF INTEREST

The Multistate Tax Commission (hereinafter referred to as the Commission) is the official administrative agency of the Multistate Tax Compact (hereinafter referred to as the Compact) entered into currently by 19 states as full members, including New Mexico, by the District of Columbia and by 12 states as associate members.[2]

The purposes of the Compact are to:

1. Facilitate proper determination of state and local tax liability of multistate taxpayers, including the equitable apportionment of tax bases and settlement of apportionment disputes.

2. Promote uniformity or compatability in significant components of tax systems.

3. Facilitate taxpayer convenience and compliance in the filing of tax returns and in other phases of tax administration.

4. Avoid duplicate taxation.[3]

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[2]The current regular members are the states of Alaska, Arkansas, California, Colorado, Hawaii, Idaho, Kansas, Michigan, Missouri, Montana, Nebraska, New Mexico, Nevada, North Dakota, Oregon, South Dakota, Texas, Utah and Washington. The associate members are the states of Alabama, Arizona, Georgia, Louisiana, Maryland, Massachusetts, Minnesota, New Jersey, Ohio, Pennsylvania, Tennessee, and West Virginia.

[3]The constitutionality of the Compact was upheld by the United States Supreme Court in *U. S. Steel, et al. v. Multistate Tax Commission, et al.*, 434 U. S. 452 (1978), affirming 417 F. Supp. 795 (S. D. N. Y. 1976). The Court there noted that the Compact ". . . symbolized the recognition that, as applied to multistate businesses, traditional state tax administration was inefficient and costly to both state and taxpayer."

In fulfillment of these objectives, the Commission and its member states have a vital interest in assuring that all businesses carrying on activities within their jurisdictions, and benefiting from governmental services and functions, bear their share of the public cost. This is not just a question of revenues, it is a question of tax justice as well.

The present case raises matters of vital concern to them. The Commission member states have a vital interest in preventing federal involvement in the business activities of private corporations from spilling over indiscriminately into state tax policies affecting the taxation of property or activities within their borders.

While we do not question the need for and the constitutional significance of implied inter-governmental tax immunity, we seriously doubt whether it should turn on the interpretation of vague and conflicting language in United States contracts with private corporations or that it should be extended to the proprietary interests. We are thus unalterably opposed to the expansion of implied government tax immunity by contractual penmanship where the consequence is not to protect vital interests of the United States Government from improper encroachment by the taxing powers of the states; but, rather, to shift national tax costs to particular geographical locations where private corporations carry on substantial business activities on behalf of the United States.

The underlying issue in this cause is whether the state of New Mexico and particular political subdivisions of that state are to bear the costs of the benefits and privileges granted the private contractors in the case at bar or whether such costs are to be borne by the United States

as a whole. For this reason, we do not believe that implied governmental immunity should be extended to exempt from non-discriminatory state taxes any private corporations which are not, in law and fact, agencies or instrumentalities of the United States. Thus, unless this Court should find in the instant case that the subsidiary and affiliated corporations of Western Electric and Santa Fe Industries, Inc. are in fact and law agencies and instrumentalities of the United States Government for all purposes, no inter-governmental tax immunity should be attributable to any of their activities.

We are particularly troubled by the position of the United States in this case that the characterization of private corporations as "procurement agents" of the United States in government contracts confers on private corporations the status of agents of the United States for implied governmental immunity tax purposes.

In conformity with the foregoing concerns, the purpose of this brief is to demonstrate to this Court why we believe the position of the United States is not supported by this Court's controlling inter-governmental tax immunity cases and is otherwise an improper extension of the doctrine of implied governmental immunity.

As to the later, we do not believe that contractual penmanship should be allowed to extend governmental tax immunity to proprietary governmental activities, particularly when these activities are conducted by private corporations which are not so assimilated as to constitute an instrumentality of the federal government.

SUMMARY OF ARGUMENT

United States v. Boyd, 378 U. S. 39 (1964) and the cases relied on therein are dispositive of this case. The legal incidences of the taxes in question and the contractual relationship between the United States and the contractors in question are not distinguishable for constitutional tax immunity purposes from the legal incidence of the tax and the contracts in the *Boyd* case. In both *Boyd* and the instant case, the legal incidences of the taxes were on the contractors, as private corporations, which were not assimilated as agencies or instrumentalities of the United States. *Boyd* and the case at bar both involved standard Atomic Energy Commission (now DOE) management contracts which were developed to facilitate the Atomic Energy Commission's substantial reliance on private industry in the construction and the management of large research and development facilities (Appellant's Brief, pp. 3, 16; *Boyd, supra*).

The reliance of the United States on *Kern-Limerick, Inc. v. Scurlock*, 347 U. S. 110 (1954) is misplaced. Unlike the case at bar and *Boyd, Kern-Limerick* did not involve the question of implied inter-governmental tax immunity under a standard Atomic Energy Commission management contract which involved ongoing business relationships between the United States and the contractors. Rather, *Kern-Limerick* involved construction contracts between the Navy and the contractors for the construction of an ammunition dump which was to be maintained and operated by the Navy. The only question in *Kern-Limerick* was whether or not the purchases of the tangible property there involved were purchases by the Navy under the Armed

Services Procurement Act of 1947 (62 Stat. 21, 42 U. S. C. (Supp. V § 157 et seq.)); see 347 U. S. at 112-113. Inasmuch as the purchases in *Kern-Limerick*, pursuant to express contract provisions and by specific purchase orders, obligated the United States to pay the vendors for the purchases, *Kern-Limerick* held that purchases made in accordance with these express provisions were purchases by the United States and thus exempt from the Arkansas gross receipts tax under the doctrine of implied governmental immunity. In *Kern-Limerick*, this governmental immunity was not destroyed by the Navy using contractors as purchasing agents in conformity with the requirements of the Armed Services Procurement Act.

Unlike the contractors in *Kern-Limerick*, the contractors here received the gross receipts in question from the United States as reimbursements for their own obligations which were not incurred in conformity with the statutes and regulations applicable to United States Procurement agents. This is particularly evident in regard to their own operating expenses, including employee salaries and fringe benefits, which involved no purchasing relationships with third parties.

The advance funding arrangement relied upon by the United States does not negate this fact. Unless the contractors in question are so assimilated as to constitute instrumentalities of the United States, it is totally illogical to conclude that the payment of their day-to-day operating expenses, including the procurement of supplies for this purpose, as well as payment of employee salaries, constitute the payment of obligations of the United States.

Since it is conceded that the contractors in question are not United States instrumentalities, but are independ-

ent, private corporations that purchased on their own account, *Boyd* and the cases relied on therein, including *Esso Standard Oil Co. v. Evans*, 345 U. S. 495 (1953); *Alabama v. King & Boozer*, 314 U. S. 1 (1941); *James v. Dravo Contracting Co.*, 302 U. S. 134 (1937); and *United States v. Township of Muskegon*, 355 U. S. 484 (1958) and not *Kern-Limerick, supra*, control disposition of this case. Furthermore, if *Kern-Limerick* conflicts with the decision below, it should be overruled because it would place form over substance and extend implied inter-governmental tax immunity beyond its legitimate scope.

THE ARGUMENT

Kern-Limerick is not controlling precedent and refutes the argument of the United States that the contractors in question are procurement agents of the United States.

In an effort to extend implied governmental tax immunity to admittedly private corporations conducting independent business activities, primarily in the form of research and development services for the DOE, the United States has contracted for so-called "advance funding" of its contractual obligations to these private corporations. Based on this contractual arrangement, United States contends that the court below erroneously concluded that this was only a means utilized by the United States to discharge its obligations under the contract to reimburse these private corporations for services rendered by them pursuant to the contracts. Rather, the United States

argues that the court below should have concluded that the advance funding arrangement converted these independent contractors into procurement agents of the United States. It then argues that the agency principle established in *Kern-Limerick* controls this case.

The basic fallacy of this position of the United States is that the source of funds for the payment of obligations or activities does not control whose obligations are being discharged or who is conducting the activities. For example, if X contracts with Y to build a building for X, and advances funds to Y to be used to construct the building, X does not become either the builder of the building or the one liable to those furnishing supplies or services to the builder. Furthermore, if state A imposes a gross receipts tax on the gross receipts of those engaged in the construction business, this tax is not imposed on Y as an agent of X because the receipts of Y are traceable to the funds of X by advanced payments, lines of credit or otherwise.

As the foregoing example illustrates, much more than advance payments, however effectuated, is required to convert the contractors in question to procurement agents of the United States. What is required, as found by this Court in *Kern-Limerick*, is that the person doing the purchasing must be able to demonstrate the following:

1. He has authority to and is acting as a purchasing agent of the United States in accordance with United States' procurement.

2. The United States is disclosed as the purchaser on the purchase order or other purchase document.

3. Title to the goods pass directly to the United States.

4. The purchasing agent assumes no liability to the seller as a result of the purchase.

The United States does not contest the foregoing in its discussion of *Kern-Limerick* (App. Br., pp. 12-13, 29). Furthermore, in arguing that *Kern-Limerick* is controlling (App. Br., p. 13), the United States does not rely on the facts held controlling in *Kern-Limerick*. Rather, as summarized on page 20 of its brief, it relies on the following facts:

1. Title passes directly to the government from the vendors;

2. Risk of loss is directly on the government;

3. The government has control over the disposition of the property and approval of management procedures employed by each contractor;

4. The advance funding arrangement.

On page four of its brief, the United States admits:

1. Under the advance funding procedure, *all contract costs are paid by the contractors* on drafts executed by the contractors.

2. Only obligations that are *"properly incurred"* by the contractors *are treated as* DOE liabilities.

Kern-Limerick stands only for the proposition that "the State may not impose a tax the legal incidence of which falls upon the federal government." *United States v. County of Fresno*, 429 U. S. 452, 459-460, n. 7 (1977). This is not the case here.

It is further noted that *Kern-Limerick* involved only one-time construction contracts while here the contracts pertain to the operation and management of complex facilities on a continuing basis. Also, in *Kern-Limerick*, the contractors were bound by the procurement requirements imposed by federal statute. Here there are no such requirements.

The controlling fact, as amplified by the brief of New Mexico, is that the contracts in question do not give the contractors the status of procurement agents of the United States nor could they do so in regard to the services directly performed by the contractors unless the contractors were, in fact and law, instrumentalities of the United States, which admittedly they are not. Furthermore, here, actual procurement was by the contractors on their own account.

As indicated on pages 31-37 of the brief of the United States, it assumes that characterization of the contractors as persons acting on behalf of the United States, and the advance funding arrangements in the contracts, without more, places the contractors in the position of procurement agents of the United States.[4] This simply does not follow. Under this reasoning, if the contracts in question recited that the sun was the moon, the United States argues that

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[4]This point is illustrated by the heading on page 21 of the United States' brief:

> "The Contracts Here Designate the Contractors as Procurement Agents of the United States Empowered to Disburse Funds belonging to the United States."

Absent from this heading is an assertion that the contractors are, in fact and law, disbursement agents of the United States. In fact, the United States concededly has stopped short of designating the contractor as agent (App. Br., p. 183; R. III).

this must be accepted as a fact. *Kern-Limerick* requires more than recitals to establish an agency relationship. *Kern-Limerick* required contract performance to conform to a true procurement agency relationship in accordance with express contractual provisions which spelled out this relationship.

As noted in *Kern-Limerick*:

> "The stipulation of facts shows in detail the course of business under this contract in the purchase of supplies and the form of this purchase. Both conform to the language of the contract in requiring specific Government approval to the purchasing agent for each request for bid and each purchase. Under these circumstances, it is clear that the Government is the disclosed purchaser and that no liability of the purchasing agent to the seller arises from the transaction." (347 U. S. 110 at 120-121)

Thus, the United States' reliance on *Kern-Limerick* and advanced funding is misplaced.[5]

Boyd and the cases cited therein control disposition of this case wherein it was held that implied inter-governmental tax immunity is limited to taxes, the legal incidences of which are imposed on agencies or instrumentalities of the United States government.

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[5]In regard to the position of the United States, it is interesting to note that it admits that the management fees in question, although subject to advanced funding, are clearly taxable by New Mexico. We fail to see how these fees are any more or less the gross receipts of the contractors than the receipts the contractors receive for payment of the salaries of their employees, or for that matter for equipment used by their employees.

It is here undisputed that the legal incidence of both the New Mexico gross receipts and compensating use tax is on the contractors (App. Br., p. 25). Nor is there any question as to the validity of these taxes as applied to the contractors in question unless they have the status of agents or instrumentalities of the United States in regard to the gross receipts in question. This Court in *Boyd*, under facts not distinguishable from the facts here, held that Atomic Energy Commission management and construction contractors were liable for the use tax for tangible personal property which was used to fulfill their obligations under Atomic Energy Commission contracts. In an effort to have the use tax declared invalid, the government argued that the contractors were agents of the United States in rendering services for the A. E. C. The Court rejected this argument by noting:

> "The help of these companies was not sought merely to supply skilled manpower for employment by the United States and it is not argued that Carbide's 12,000 men have somehow become employees of the Commission rather than of Carbide. See *Powell v. United States Cartridge Co.*, 339 U. S. 497; *Mahoney v. United States*, 216 F. Supp. 523 (D. C. E. D. Tenn.). Of course there are governmental directives and instructions which must be obeyed, for the Commission decides the uses of and needs for fissionable material; and, of course, in the sensitive area of atomic energy operations the Commission's controls are subject to modification and change in the light of technical and other developments. But Carbide and Ferguson brought to the Oak Ridge operation both skill and judgment the United States needed and did not have and there is substantial room for the exercise of both, within and without the broad directives issued by the Commission. Should the Commission intend to build or operate the plant with its own servants and em-

> ployees, it is well aware that it may do so and familiar with the ways of doing it. It chose not to do so here. We cannot conclude that Carbide and Ferguson, both cost-plus contractors for profit, have been so incorporated into the government structure as to become instrumentalities of the United States and thus enjoy governmental immunity. (378 U. S. 47-48; footnote omitted)

Boyd is not distinguishable. Here, the contractors have received gross receipts for the construction, operation and management of atomic energy facilities. They are no more agencies or instrumentalities of the United States than the *Boyd* contractors. This is particularly true in regard to the gross receipts the contractors receive for the services rendered by their own employees which were disassociated from transactions with third parties. It is also true in regard to the gross receipts they received as reimbursements for expenditures to third parties, since the contractors were not procurement agents of the United States within the purview of *Kern-Limerick* because they furnished and purchased goods and services on their own account.

Any doubt about *Boyd* as precedent here is removed by the cases relied upon in *Boyd*, particularly *Alabama v. King & Boozer, supra.* In *Boozer*, the court upheld a retail sales tax on contractors as purchasers of tangible personal property inasmuch as the legal incidence of the tax was on the contractors and not the United States and inasmuch as the contractors were not agencies or instrumentalities of the United States. To like effect is *Curry v. United States*, 314 U. S. 14 (1941), *Esso, supra* and *Muskegon, supra.* The controlling question in each of these cases was whether the legal incidence of the tax was

on the United States. A determination of whether the contractors were agencies or instrumentalities of the United States was relevant only for this purpose. The same is also true in regard to *Kern-Limerick*.

Boyd also lays to rest the significance here of *United States v. Livingston*, 179 F. Supp. 9 (1959), aff'd per curiam, 364 U. S. 281 (1960). *Boyd* limited this Court's affirmance of *Livingston* to its peculiar factual underpinnings which are not relevant here. Unlike *Livingston*, there is here no claim that neither the contractors nor their controlling parent corporations received no benefit or commercial advantage as a result of the contracts in question.

In sum, properly construed in light of the facts of this case, *Boyd*, and not *Kern-Limerick*, is dispositive of this case.

There is no valid reason why the judicial doctrine of implied governmental tax immunity should be extended to embrace the activities of private corporations which conduct proprietary activities on behalf of governmental agencies unless such private corporations are agencies and instrumentalities of the United States government.

The United States has cited no policy reason and the court below found no reason why the doctrine of implied governmental immunity should extend to the private corporations in question. Admittedly, the taxes in question are non-discriminatory and are directly imposed on private corporations as a result of their own commercial activities in the state of New Mexico. There is no claim here by the United States that these taxes unduly interfere

with functions of the United States Government in carrying out its atomic research and development programs. The fact that the taxes in question do not do so, at least in the eyes of Congress, is exemplified by its repeal of Section 9 (b) of the Atomic Energy Act by the Congress.[6] Absent such interference, within the purview of the doctrine of implied governmental tax immunity first enunciated in *McCullough v. Maryland*, 17 U. S. (4 Wheat.) 316 (1819) there is no valid basis for application of the doctrine of implied inter-governmental tax immunity. This does not mean that undue interference may not be implied where state taxes are imposed on the possessions, institutions and activities of the federal government itself. It does mean that such immunity should not be implied in circumstances where state taxes are not so imposed.

While acknowledging that the contractors in question are not agencies or instrumentalities of the United States within the purview of *McCullough v. Maryland, supra*, or otherwise, the United States is here attempting to extend the agency or instrumentality doctrine to include an admittedly implied limited agency relationship in reference to particular activities and then argue that state taxes which are imposed on these activities constitute taxes on a federal agency or instrumentality. This conclusion does not follow. Furthermore, no such extension of implied governmental tax immunity is justified. It adds uncertainty and generates litigation in the implied tax immunity area, which is costly to the government and the

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[6]For an explanation of the repeal of Section 9 (b) of the Atomic Energy Act, see Footnote 9 in the brief of the United States, pages 26-27

states. Furthermore, it is subject to contractual penmanship and places the contractual form over economic and business substance.

For the above stated reasons, it is respectfully submitted that implied inter-governmental tax immunity should not be extended to private corporations which are not assimilated into the structure of United States Government as its agencies or instrumentalities.

CONCLUSION

This Court should affirm the judgment of the court below. In so doing, it is respectfully requested to affirm the proposition that only those taxpayers that constitute federal agencies and instrumentalities, in fact and law, are to be accorded implied immunity from state taxation. This affirmation is simply the reflection of the notion that private corporations carrying on commercial activities with the federal government cannot, by inference and contractual manipulation, stand in the shoes of the United States for constitutional tax immunity purposes. In no event should the Court extend *Kern-Limerick* to the distinguishable facts and circumstances of this case.

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No. 80-702

IN THE

Supreme Court of the United States

October Term, 1980

UNITED STATES OF AMERICA, *Petitioner,*

v.

STATE OF NEW MEXICO, *et al., Respondents.*

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE TENTH CIRCUIT

BRIEF ON BEHALF OF THIRTY-SIX STATES AS AMICUS CURIAE FOR THE STATE OF NEW MEXICO

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QUESTIONS PRESENTED

1. Whether three private corporate contractors performing contracts for the United States Atomic Energy Commission ("AEC") and its successors are subject to the New Mexico gross receipts and compensating taxes (§§72-16A-1, *et seq.*, N.M.S.A. 1953) on funds received under their contracts to pay salaries and related costs of their own employees, their own award fees, and obligations to third party suppliers from whom they have ordered in their own names.

2. Whether reliance by three private corporate contractors on an "advanced funding" arrangement pursuant to 41 U.S.C. §255, §4(c)(2) of the Atomic Energy Act of 1946, now codified at 42 U.S.C. §2061(b), and 31 C.F.R. Part 205 (1976), to finance their performance of contract work for the Atomic Energy Commission, renders such contractors federal agents exempt from the New Mexico gross receipts tax, where the funds are used to meet the contractors' obligations, not those of the federal government.

3. Whether, in the absence of Congressional authorization, agency-creating clauses inserted in contracts with three private corporate contractors performing work for the Atomic Energy Commission, insulate them from the New Mexico gross receipts and compensating taxes.

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INTEREST OF THE AMICUS CURIAE

Private corporations under contract to federal agencies, including the Atomic Energy Commission and its successors, perform their work in virtually every state of the country. Litigation challenging the right of the individual states to levy a variety of taxes on such contractors has arisen in virtually every state as well. The determination in the present case will have repercussions on each state's revenues and tax structures. More importantly, it may avoid future litigation by defining

the reach of the taxing authority of the states and the scope of the federal government's power to insulate private corporations from state taxes.

In the present case, the United States argues that all contractors utilizing advanced funding arrangements for their financing are federal agents, rather than identifying special contract provisions or circumstances which render particular Atomic Energy Commission contractors agents, U.S. Brief, 28, 33. This is a broad incursion on the general right of states to levy non-discriminatory taxes on federal contractors, in purported compliance with the narrow exception enunciated in *Kern-Limerick, Inc. v. Scurlock*, 347 U.S. 110 (1954). The attempts of federal contracting officials to insert agency-creating clauses in the contracts at issue here further necessitate a reconsideration of the validity of the *Kern-Limerick* holding. These, too, are issues impinging directly on each state.

Amicus curiae adopt the presentation of the opinion below, the statutes involved, and the statement of the case, contained in the brief of the State of New Mexico.

ARGUMENT

I. UNLESS SPECIFICALLY FORBIDDEN BY CONGRESS, THE STATES SHOULD BE FREE TO LEVY NON-DISCRIMINATORY TAXES ON FEDERAL CONTRACTORS.

In the seminal case of *M'Culloch v. Maryland*, 17 U.S. (4 Wheat.) 316 (1819), this Court recognized that its blanket prohibition of state taxation of federal activities might

> not extend to a tax paid by the real property of the bank, in common with the other real property within the State, nor to a tax imposed on the interest which the citizens

> of Maryland may hold in this institution, in common with other property of the same description throughout the State.
>
> *Id.*, at 436.

Thus, the validity of non-discriminatory taxes on federal activities and instrumentalities was affirmed even in the case which barred virtually all state taxation of such activities. The validity of non-discriminatory taxes was at the heart of this Court's decision in *James v. Dravo Contracting Company*, 302 U.S. 134 (1937), in which the prohibitions of *M'Culloch v. Maryland* were essentially swept away in regard to federal contractors. The validity of non-discriminatory state taxation of those working for the federal government was again highlighted in *United States v. County of Fresno*, 429 U.S. 452 (1977), where this Court approved the above quote from *M'Culloch v. Maryland*, 429 U.S. at 459, noting that

> "[f]or many years the Court read the decision in M'Culloch as forbidding taxes on those who had contractual relationships with the Federal Government. . . In later years, however, the Court departed from this interpretation of M'Culloch,
>
> *Id.*, at 460.

Thus, this Court has come close to adopting the observation that

> One could, and perhaps should, read M'Culloch . . . simply for the principle that the Constitution prohibits a state from taxing discriminatorily a federally established instrumentality,
>
> *First Agricultural National Bank v. State Tax Commission*, 392 U.S. 339, 350 (1968) (Marshall, J., dissenting).

This Court's decision in *Kern-Limerick, Inc. v. Scurlock*, 347 U.S. 110 (1954), cannot be reconciled with the cited line of cases. It permits the Executive Branch to unilaterally insulate

itself from the economic burden of a non-discriminatory state tax whose legal incidence falls on a federal contractor. Furthermore, *Kern-Limerick* reads into the general power of executive agencies to contract, a Congressional intent that such contracts may insulate the contractors from state taxes. In reality, Congress has been silent in this regard. As this Court has held,

> It is true that the silence of Congress, when it has authority to speak, may sometimes give rise to an implication as to the Congressional purpose. . . but there is little scope for the application of that doctrine to the tax immunity of governmental instrumentalities.
>
> *Graves v. New York*, 306 U.S. 366, 479-480 (1939).

The judiciary must be ever vigilant to protect the United States from discriminatory taxation which invades its supremacy by denying equal protection to its contractors. However, we urge that this Court reconsider *Kern-Limerick, Inc. v. Scurlock* and hold that, absent an affirmative showing of Congressional intent to insulate private contractors, they are liable for non-discriminatory state taxes.

II. *KERN-LIMERICK, INC. v. SCURLOCK* REQUIRES AFFIRMATIVE DESIGNATION OF CONTRACTORS AS FEDERAL AGENTS IN ORDER TO INSULATE THEM FROM STATE TAXES.

In the present case, the United States contends that these three contractors are agents not by virtue of specific authorizations but by virtue of their reliance on an advanced funding arrangement, U.S. Brief, 28, 33. Since the Atomic Energy Commission has over 160 other contractors financed through the same arrangement, the United States' contention is not that

these three contractors are uniquely entitled to exemption but that all of its large contractors are insulated, R.VI, McGrath depo. 9. Even if this Court recognizes the continuing validity of *Kern-Limerick, Inc. v. Scurlock, supra,* the United States cannot prevail. *Kern-Limerick* could not be clearer in requiring express, affirmative designation of particular contractors. Here, the United States argues for blanket immunization of all large Atomic Energy Commission contractors. This is a complete distortion of *Kern-Limerick* and should be rejected.

The voluminous discovery conducted by the State of New Mexico compellingly illustrates that advanced funding is not unique to the Atomic Energy Commission, has never been regarded as an agency-creating device within the Atomic Energy Commission, and in its operation does not bind the United States to third parties, N.M. Brief, 24-29. Had this factual development occurred in *Livingston v. United States,* 364 U.S. 281 (1960), *aff'g,* 179 F.Supp. 9 (E.D.S.C. 1959), *United States v. Nevada Tax Commission,* 291 F.Supp. 530 (D. Nev. 1968), *aff'd,* 439 F.2d 435 (9th Cir. 1971), and the sales tax portion of *United States v. Boyd,* 211 Tenn. 139, 363 S.W.2d 193 (1962), *aff'd on another issue,* 378 U.S. 39 (1964), the decisions in those cases might well have been in favor of the state taxing authorities. In addition, the record in the present case indicates that the Atomic Energy Commission does not regard its management contractors as agents absent express authorization, N.M. Brief, 20-23. In the present case, even the July 1, 1977, contract amendments do not amount to an express authorization but rather a series of legal arguments, J.A. 64.

The drafting of these contract amendments evidences the cynicism of the Executive Branch in regard to insulating its contractors. Its interpretation of *Kern-Limerick* as a license to insert the barest minimum of supposedly operative phrases,

while preserving a non-agent status in all areas apart from taxation, could not be clearer. Even more disturbing is the discussion in New Mexico's brief concerning the Department of Defense which, in presentations to Congress, repudiated the *Kern-Limerick* holding but continued to argue its impact in court after court thereafter, N.M. Brief, 43-44. Eliminating immunity for federal contractors absent explicit Congressional authorization will end the Executive Branch's dubious role as guardian of the federal-state balance in taxation.

Reaffirming the application of non-discriminatory taxes to federal contractors will not produce a massive drain on the federal treasury. Only seven states have a tax on the gross receipts of contractors rendering services which is equivalent to New Mexico's gross receipts tax.[1] In these states, constituting a contractor as an agent would presumably bar taxation of its receipts. Contractors in all other states would be unaffected by an agency designation since their receipts are not taxed anyway.

Although there would be a somewhat greater effect with regard to taxation of suppliers selling property to federal contractors, nonetheless, more than half of all states would immunize or tax these transactions regardless of the agency designation. In sixteen states, constituting a contractor as an agent would not change its tax burden in regard to such purchases, either because these states do not have a sales or comparable tax,[2] because sales to federal contractors are

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[1] Arizona; Ariz. Rev. Stat. Ann. §§42-1309, 42-1361 and 42-1371; Mississippi (as to construction only), Miss. Code Ann. §27-65-21, M.C.A. 1972; South Dakota, S.D. Comp. Laws Ann. §10-45 *et seq.*; Virginia, Va. Code §58-441.1 *et seq.*; Washington, Wash. Rev. Code Ann. §82.04.010 *et seq.*; West Virginia, W.Va. Code §11-13-2 *et seq.*; Delaware, Del. Code Ann., tit. 30, §2501 *et seq.*

[2] Alaska, Montana, New Hampshire and Oregon.

exempt even if they are not agents,[3] because sales of tangible personal property are exempt if resold to the United States,[4] because a claim for refund of tax paid by the federal contractor may be made by the United States[5] or because they place the legal incidence on the seller and have no statutory exemption for transactions with the federal government or its agents.[6]

Additionally, fifteen states would immunize the sale of at least some types of tangible personal property to federal contractors pursuant to statutory exemptions applicable to sales of goods which are subsequently resold.[7]

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[3] Hawaii, Hawaii Rev. Stat. R.S. §237-26; Kansas, Kansas Stat. Ann. §79-3606(e) (1980 Supp.); Nevada, Nev. Rev. Stat. §§372.390, 372.345; New Jersey, N.J. Stat. Ann. §54:32 B-9; New York (as to tangible personal property incorporated into a building or structure owned by the United States), N.Y. Tax Law §§1115(15), 1115(16) (Consol.); Ohio (as to building or construction materials incorporated into a structure built under contract with the United States), Ohio Rev. Code Ann. §§5739.01, 5739.02; Florida, Department of Revenue Rule 12A-1.51(7), Florida Administrative Code.

[4] Texas, Tex. S. Tax Code Ann. §20.04 (Vernon); Nebraska, Neb. Rev. Stat. §77-2704(1)(a) R.S. Supp., 1980.

[5] North Carolina, Dept. of Revenue Sales Tax Regulation 42.

[6] South Carolina, S.C. Code §12-35-510; and California (as to leases of tangible personal property to the United States), West's Ann. Rev. and T. Code §6381.

[7] Arizona (as to construction materials), Ariz. Rev. Stat. Ann. §42-1321 A(3); Arkansas, Ark. Stat. Ann. §84-1904(5); Colorado (as to construction materials), Colo. Rev. Stat. §39-26-114(XIX); Georgia, Ga. Code Ann. §91A-4501(f)(1); Indiana (as to materials for manufacturing), Ind. Code §§6-2.55-5, 6-2.55-6; Maine (as to tangible personal property used in research and development and as to machinery and equipment used in manufacturing), Me. Rev. Stat. Ann. 36 §§1760(31), 1760(32); Massachusetts (as to construction materials used in government construction contracts), Mass. Gen. Laws Ann. Ch. 64 H§6(f); Michigan, Mich. Comp. Laws

(Cont. p. 8)

CONCLUSION

The decision of the Court of Appeals for the Tenth Circuit should be affirmed.

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(Cont. p. 9)

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[7] (Cont. from p. 7)
§205.51; Missouri (as to materials for manufacturing), Mo. Ann. Stat. §144.030(6); Oklahoma, Okla. Stat. Ann. tit. 68 §1305(o); Pennsylvania, Pa. Stat. Ann. tit. 72 §7204 (Purdon); Tennessee (as to materials for manufacturing), Tenn. Code Ann. §67-3004; Utah (only retail sales are taxed, not wholesale sales), Utah Code Ann. §59-15-4; Vermont (as to materials for manufacturing), Vt. Stat. Ann. tit. 32 §§9701, 9741; Virginia, Va. Code §58.441.6.

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